



## **EFFECT OF CORPORATE GOVERNANCE ON FINANCIAL PERFORMANCE OF STATE FUNDED ENTITIES IN KENYA**

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**Abstract:** Corporate governance is generally described as simply the system by which companies or public bodies are: directed, and controlled. For any public entity not to collapse, they ought to comply with Corporate Governance principles including but not limited to: Appointments, Team composition, Control procedures and processes and Performance management and assessment. In Kenya these ideals are never implemented optimally. The main objective of the study was to analyze the effects of corporate governance on financial performance of state funded entities in Kenya. Specifically the study focused on the following elements of corporate governance: autonomy status, board effectiveness, government supervision and regulations overlap on performance of the state owned entities in Kenya. The study adopted descriptive cross-sectional design. The study targeted the board of directors, directors, senior managers, finance and accounts staff of Kenya Broadcasting Corporation, Kenya Electricity Generating Company, Kenya Pipeline Company, Kenya Railways Corporation, National Oil Corporation of Kenya and Kenya Broadcasting Corporation. The data generated by the study after fieldwork was edited, coded then entered into a computer for processing using the Statistical Package for Social Sciences (SPSS v.21.0). Descriptive and inferential statistics was used to analyze information generated from respondents. The data collected was presented by use of percentages, frequency distributions, tables, and the researcher categorized variables. The study concluded that, holding all the other factors constant, the financial performance in the state owned entities in Kenya was tested against key corporate governance elements measured by their significance and established that in deed the corporate governance elements (Autonomy Status (AS), Government Supervision (GS), Regulations Overlap (RO), and Board Effectiveness (BE)) contributed to 80.8% of the variation of financial performance in the state owned entities in Kenya as explained by adjusted R<sup>2</sup> of 0.808. The study finally, recommended that, there is a need to streamline the overlapping regulations in order to give parastatals some autonomy, which would enable them to meet targets set under the performance contracts they have entered into with the government.

**Keywords:** Autonomy status, Corporate governance, Financial performance, Regulations overlap

### **Introduction**

Corporate governance refers to the mechanism which guarantees that the affairs of a corporate body are conducted in order to serve and protect the individual and collective interests of all stakeholders (Maria & Thomas, 2012). Makki, (2013) argues that, corporate governance decrees that while a firm is achieving its goal of shareholder's wealth maximization, this achievement should not be at the expense of other stakeholders.

According to Agrawal and Knoeber, (2006) effective and efficient management of public sector organizations is an issue of concern in many countries. Chiara, (2010) argues that, public sector organizations are increasingly being held more accountable for their performance and are therefore

expected to operate efficiently and effectively. This means that public sector organizations have to search for ways to improve on their activities. Notable approaches include the use of performance contracts. Makki, (2013) similarly argues that, activity based management practices can increase transparency and efficiency when conducting government activities thereby assisting public sector organizations to achieve their objectives

Historically, some public sector enterprises were formed to create employment for large numbers of people. However, in recent years, public sector management has become increasingly results and customer-focused (Abdullah & Page, 2009). They argue that, this can be partly attributed to a growing unwillingness among many communities and governments to accept the continuation of historic commitments simply because they are historic. According to Agrawal and Knoeber, (2006), some countries have also noticed diminishing differences between the private and public sectors. For instance, private sector organizations are now expected to take more social responsibility measures while the public sector is witnessing the need to focus on customers and to justify their existence. The contemporary business environment pays great attention to target, measurement, accountability, productivity gains and the continued relevance and value of specific activities or programs.

In Kenya, government owned entities (GOE's) have been established and played these roles in diverse ways. The experience has been in some cases successful and in others not so. In the recent past Kenya has set itself an ambitious, but achievable development agenda, reflected in Vision 2030. This is further articulated in its Second Medium Term Plan, 2013 – 2017, which is the key implementation instrument. Faced with a challenging and fluid regional as well as global context, it is clear that it cannot be business as usual, that is if the country is going to quickly and effectively address development challenges, it will require significant transformation in the way it identify and apply, inter alia, people, natural, financial and organizational resources. One of the key policy instruments that governments world over have applied in supporting national development have been GOEs, in Kenya referred to variously as parastatals, state corporations or semi-autonomous government agencies in some cases. (Report of the Presidential Taskforce on Parastatal Reforms, 2013).

The proper management of public sector organizations is therefore an issue of concern in developed and developing countries (Abdullah & Page, 2009) Garratt, (2013) contends that, many African economies began to pay particular attention to the ideals of good governance in the beginning of the 1980s. Corporate governance systems have evolved in a number of developing African countries. Nevertheless, Johanson & Ostergren, (2010) argues that the concept of corporate governance is not necessarily the best solution for developing economies. This is because a number of developing countries face numerous problems that include unstable political regimes, low per capita incomes and diseases. Such problems require more elaborate solutions than simply adopting corporate governance concepts.

### **Problem Statement**

In the wake of corporate financial scandals and failures, there is an ever increasing attention on corporate governance issues. State funded organizations are deeply implicated in most fiscal problems of African governments because of their inefficiency, losses, budgetary burdens, and provision of poor products and services. According to Mulili, (2011) developing countries are often faced with a multitude of problems that include uncertain economies, weak legal controls, protection of investors and frequent government intervention. He further highlights that, these problems make it even more necessary for developing countries to adopt effective corporate governance structures. The pressures of an increasingly globalized world economy, democratization, IMF/World Bank's economic reforms and

the recent financial scandals in the West have forced a number of developing countries to adopt the corporate governance ideals.

According to United Nations Development Program (2010), improved corporate governance systems can serve as an incentive for attracting foreign investment. In fact, it is poor economic performance and high international debt levels in emerging markets that forced the World Bank, IMF, and the IFC to intervene in an effort to improve the corporate governance systems of these markets. A number of developing countries have embraced the corporate governance ideals. However, developing countries practice corporate governance models that are different from the models adopted by developed countries (Mulili, 2011). This is partly due to the unique economic and political systems found in developing countries.

According to David, (2009), corporate governance structures in developing countries are weak. In Kenya these systems are at their weakest and this prompts this research work. A review of existing literature shows that the researchers have not reached any definite consensus and establish the impact of corporate governance on financial performance (Mulili, 2011). These gaps prompted the researcher to analyze the effects of corporate governance on financial performance of state funded entities in Kenya

The specific objectives of the study were;

- i. To establish whether the autonomy of state funded organizations in Kenya influences their financial performance
- ii. To determine the extent to which board effectiveness of the state funded organizations in Kenya affect their financial performance
- iii. To find out the influence of government supervision on financial performance of the state owned entities in Kenya
- iv. To establish the effect of regulations overlap on financial performance of the state owned entities in Kenya

### **Theoretical review of the study**

Existing literature identifies a number of theories in corporate governance and financial performance. A better understanding of corporate governance management is essential for the any corporate success. This study was thus guided by three theories namely; Agency theory, contingency theory and Resource Dependency Theory.

#### **Agency Theory**

Agency theory is concerned with resolving problems that can exist in agency relationships; that is, between principals such as shareholders and agents of the principals for example, company executives. The two problems that agency theory addresses are: the problems that arise when the desires or goals of the principal and agent are in conflict, and the principal is unable to verify what the agent is actually doing and the problems that arise when the principal and agent have different attitudes towards risk. Because of different risk tolerances, the principal and agent may each be inclined to take different actions (Anthony & Nicholas 2006).

Adams (2004) in his article stated that agency theory can provide for richer and more meaningful research in the internal audit discipline. Agency theory contends that internal auditing, in common with other intervention mechanisms like financial reporting and external audit, helps to maintain cost-

efficient contracting between owners and managers. Agency theory may not only help to explain the existence of internal controls and internal audit in firms but can also help explain some of the characteristics of the internal audit department, for example, its size, and the scope of its activities, such as financial versus operational auditing. Agency theory can be employed to test empirically whether cross-sectional variations between internal auditing practices reflect the different contracting relationships emanating from differences in organizational form.

### **Contingency Theory**

Contingency theory is an approach to the study of organizational behavior in which explanations are given as to how contingent factors such as technology, culture and the external environment influence the design and function of organizations. The assumption underlying contingency theory is that no single type of organizational structure is equally applicable to all organizations. Rather, organizational effectiveness is dependent on a fit or match between the type of technology, environmental volatility, the size of the organization, the features of the organizational structure and its information. Contingency theories were developed from the sociological functionalist theories of organization structure such as the structural approaches to organizational studies by (Woods, 2009).

Contingency theory is used to describe the relationships between the context and structure of internal control effectiveness and organizational performance, especially reliability of financial reporting. Empirical study suggests that internal auditors who are specialized and higher in internal audit ability will achieve internal control effectiveness analysis and that the firm will benefit from the organizational effectiveness via internal control mechanism efficiency (Cadez & Guilding, 2008).

Cadez and Guilding (2008) identified some factors, which impact management controls; these are: external environment, technology, structure and size, strategy and national culture. It suggests that the demands imposed by technical tasks in the organization encourage the development of strategies to coordinate and control internal activities. The location of information in relation to technology and environment has an important influence on organization structure. In uncertain environments with non-routine technology, information is frequently internal. Where environments are certain, or where technology is routine, information is external. The dimensions of structure and control include authority structure and activities structure that is rules and procedures that determine the discretion of individuals. Authority relates to social power. In the contingency model, decentralized authority is more appropriate where uncertain environments or non-routine technology exist. Centralized authority is more appropriate when environments are certain.

### **Resource Dependency Theory**

The basic proposition of resource dependence theory is the need for environmental linkages between the firm and outside resources (Johanson & Ostergren, 2010). In this perspective, directors serve to connect the firm with external factors by co-opting the resources needed to survive (Bacon, 2013). Thus, boards of directors are an important mechanism for absorbing critical elements of environmental uncertainty into the firm.

Donaldson & Davis, (2011) held that environmental linkages or network governance could reduce transaction costs associated with environmental interdependency. The organization's need to require resources and these leads to the development of exchange relationships or network governance between organizations. Further, the uneven distribution of needed resources results in interdependence in organizational relationships. Several factors would appear to intensify the character of this

dependence, e.g. the importance of the resource(s), the relative shortage of the resource(s) and the extent to which the resource(s) is concentrated in the environment (Donaldson and Davis, 2011)

Additionally, directors may serve to link the external resources with the firm to overwhelm uncertainty (Bacon, 2013), because managing effectively with uncertainty is crucial for the existence of the company. According to the resource dependency rule, the directors bring resources such as information, skills, key constituents (suppliers, buyers, public policy decision makers, social groups) and legitimacy that will reduce uncertainty. Thus, Hillman and Dalziel, (2013) consider the potential results of connecting the firm with external environmental factors and reducing uncertainty is decrease the transaction cost associated with external association. This theory supports the appointment of directors to multiple boards because of their opportunities to gather information and network in various ways (Donaldson and Davis, 2011)

In summary, Agency theory shows the relationship between the principal and agent and the agent's responsibilities which include financial reporting, budgeting and providing any other additional information to the principal. The contingency theory on the other hand explains that organizations' behavior and functions are dependent on factors such as technology, culture and the external environment that the organizations operate in while the theory of the firm asserts that, the firm aims to answer these questions: Existence, Boundaries, and Organization, why are firms structured in such a specific way.

### **Empirical Review**

Miring'u (2011) indicate that in early 2000, many governments in Africa had recognized the fact that State Corporations (SC's) were performing poorly. Poor SCs performance was associated with labor rigidities in the market, increased fiscal and foreign debt and inflation problems. Parastatals provided poor and unreliable services, failed to meet demand and were lagging behind in technology areas like telecommunications. Mismanagement, bureaucracy, wastage, pilferage incompetence and irresponsibility by 21 directors and employees are the main problems that have made SCs to fail to achieve their objectives.

### **The autonomy status of state funded organizations**

In order for a business entity to thrive, the approach to compliance needs to be that which inspires the spirit of enterprise (Mwaura, 2010). According to Kiser (2011), to run a business/enterprise, management must be accorded ample power to manage, but to run it effectively, it must be held accountable for the use of this power. In Kenya, although parastatals do not have autonomy, some, such as Kenya Power and Lighting, manage to remain in business due to lack of competition and heavy tariff protection, subsidies, and other special privileges. These privileges, in turn, make it impossible for other companies to compete effectively with parastatals. In fact, most of the seed companies in Kenya have already sought liberalization of the seed sector in order to end the monopoly of the Kenya Seed Company.

Miring'u (2011) argues that, since the board of directors is made responsible for the proper management of the affairs of parastatals, it is accountable for funds and responsible for the financial business and the management of the parastatal. However, unlike private companies, the ultimate internal control of parastatals lies in the government. The government performs the role of the general meeting by appointing directors and issuing directives. The Inspector of State Corporations plays an important role in the running of parastatals, as he has the duty of advising the government on all matters affecting the effective running of state corporations. He is also obliged to report to the Minister

in respect of management practices within any corporation and to report, to the Controller and Auditor General (Corporations), any cases where moneys appropriated by Parliament are not being applied by the state corporation for the purposes for which they were appropriated. Upon conclusion of investigations, the Inspector has powers to disallow any item of account that is contrary to the law or to any direction lawfully given to a state corporation. He can also surcharge the amount of any expenditure on the person responsible for incurring the expenditure.

### **Board Effectiveness**

Fresh corporate governance scandals in various parts of the world have again put the spotlight on board of directors. For instance Enron, WorldCom, Tyco International in the United States, HIH insurance in Australia, Parmalat in Italy, Saytem in India and Air New Zealand's disastrous experience with Ansett Australia highlighted the inadequate role played by the boards and failure of corporate governance processes (France & Carney, 2012). The public uproar after the Enron collapse led to enactment of The Sarbanes-Oxley Act 2002<sup>6</sup> in the US (Moeller, 2014) and similar regulations or corporate governance codes in many other countries.

According to KPMG, (2014) the pressure is now on boards to live up to their responsibilities and reduce or eliminate corporate governance abuses. In the last few years there has been more pressure on boards to show how they govern and add value to their companies. How to enhance board effectiveness has become a focus of attention and debate amongst corporate governance experts and researchers. There has been renewal of interest in understanding the roles of boards and top management and how they could be made more effective. First, there has been a deep sense of dissatisfaction amongst shareholders regarding the poor performance of corporations, raising questions about the competency of boards, corporate greed and falling shareholder value. Second, there has been a phenomenal growth in the number of institutional investors such as pension funds, mutual funds, banks, and insurance companies, who have the necessary resources and expertise to perform their fiduciary duty of ensuring good governance and returns by monitoring the board decisions. Third, there has been an increasing realization on the part of corporations that a good board is a source of strength in several ways such as attracting investment capital, improving valuations and share price performance, and providing better long-term shareholder returns.

### **Government Supervision**

Recent corporate scandals have led to public pressure to reform business practices and increase regulation (Kisero, 2011). Kisero (2011), highlights that this is a clearly manifestation of dishonesty, greed, and cover-ups in misappropriation of funds by some state corporation officials. In both the private and the public sector, there is a trend towards ever increasing demand for accountability and transparency as well as an ever increasing awareness of the necessity for having checks and balances. Governance and associated subjects have become, both explicitly and implicitly, important issues for business, government, politics, and last but not least for the general public. That is why governance should be in place in both the private sector as well as the public sector. According to Global Integrity (2007) internal processes in African government institutions are mostly outdated and highly ineffective in as far as identifying business risks to enable prevention or mitigation from its occurrence. Due to the long bureaucratic processes otherwise involved in improving government processes, the controls are slow in keeping up with the fast-paced contemporary business environment. Matters are made worse by the advent of information technology as a central tenet of modern business dealings.

KPMG, (2014), highlights that, on Mar 25 – President Uhuru Kenyatta signed an executive order requiring all parastatal board members to be recruited using criteria set out in a new code of

governance for State corporations titled “*Mwongozo*”. The criteria is meant to address the problem of bloated parastatal boards, ensure efficient running of State corporations and to avoid conflict of interests where board members bid for tenders in their own corporations. It was argued that all existing parastatal board vacancies would now be filled using this criteria which also seeks to avoid overlapping in the roles of parastatal CEOs and board secretaries since It gives criteria for appointments and reappointments to boards as well as removals, rewards and sanctions and performance management

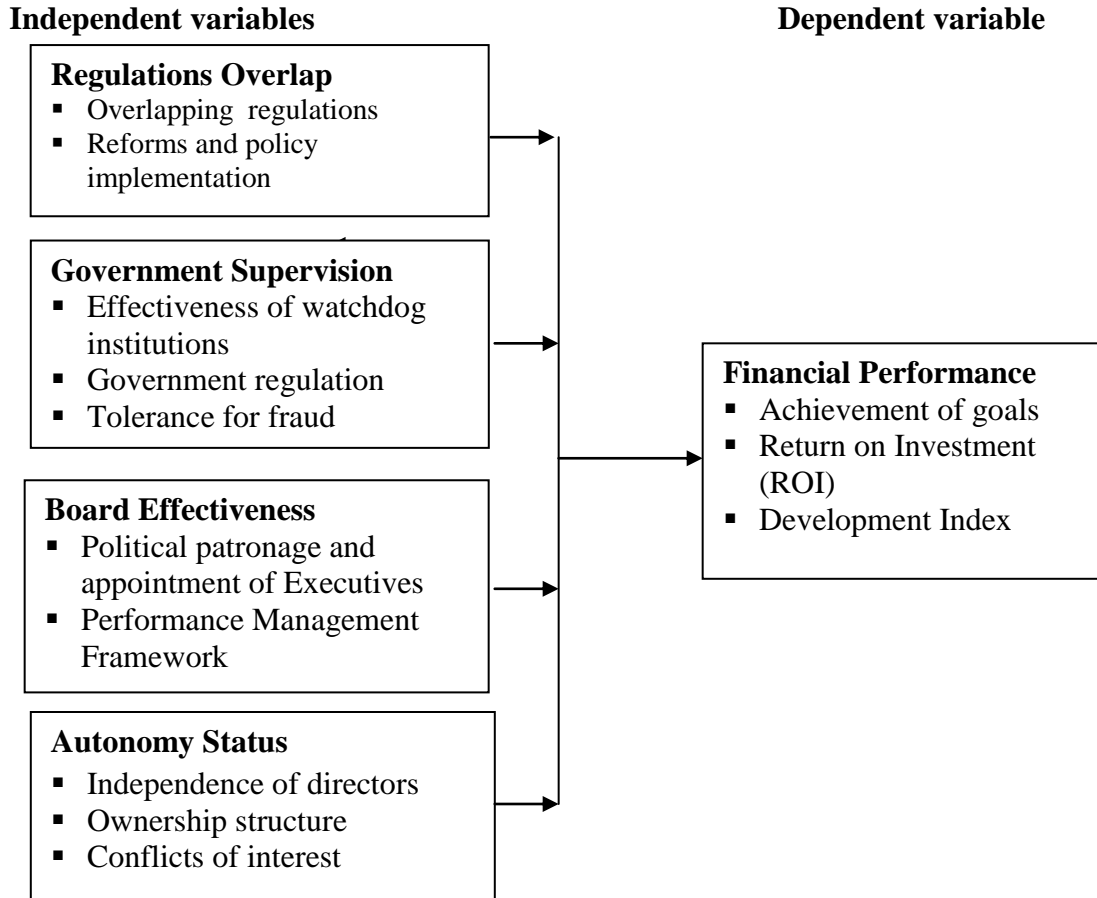
### **Regulations Overlap**

Regulation overlap in state owned enterprises refers to the method of providing regulation service in which the Balancing Authority providing the regulation service incorporates another Balancing Authority's actual interchange, frequency response, and schedules into providing Balancing Authority's AGC/ACE equation (Kihara, 2006). Parastatals are subject to overlapping regulations (Kihara, 2006). For instance, although all directors and chief executives of the Communications Commission of Kenya ("CCK") are appointees of the minister under the Kenya Communications Act, CCK is still governed by the State Corporations Act 1986 because it is a state corporation. As such, the President is empowered by the State Corporation Act to appoint the chief executives.

Additionally, parastatals are subject to direct regulation by Parliament. Parliament scrutinizes them under the legislation that establishes them. In most cases, the government exercises control of parastatals through ministers. Since all state corporations fall under a ministry, a minister has powers to give directions of a general character to the organization. Such directions may, for instance, be in relation to matters affecting a national interest; in such a situation, a minister shall determine what constitutes a national interest. Unlike private companies, where a board of directors sets the objectives of the company, the ministers are responsible for identifying such objectives in parastatals (United Nations Development Program, 2010). According to OECD, (2014) state corporations are bestowed with the responsibility of setting both commercial and non-commercial objectives. The parastatal board must answer to the ministers who are in turn accountable to Parliament. As such, accountability of directors is limited to the financial performance of parastatals. Additionally, excessive regulations, coupled with extensive ministerial intervention in the functioning of the boards, tend to impair their ability to make commercially sound decisions. Parastatals, including the ones with specific enabling legislation, are required to: report directly to the parent ministry because the ministry, in conjunction with the Treasury, must approve parastatal establishment and the remuneration system; obtain budget and investment approval from the Treasury; and justify their accounts before the Public Accounts Committee of Parliament. Also, parastatals are subject to review by the State Corporations Advisory, the Controller, the Auditor-General, and the Inspector-General (Corporations).

### **Conceptual Framework**

The independent variables in this study were autonomy, board effectiveness, government supervision and regulations overlap. The dependent variable was financial performance of the state owned entities in Kenya.



**Figure 1: Conceptual Framework**

### Research Methodology

A descriptive cross-sectional design was employed in this study. The study targeted the board of directors, directors, senior managers, finance and accounts staff of Kenya Broadcasting Corporation, Kenya Electricity Generating Company, Kenya Pipeline Company, Kenya Railways Corporation, National Oil Corporation of Kenya and Kenya Broadcasting Corporation. The study adopted a purposive random sampling technique justified by the fact that it provides researchers and statisticians with a degree of control and sense of process. Out of the targeted 360 respondents, 30% of respondents will be sampled from each targeted State Owned Enterprise. According to Mugenda and Mugenda (2005), a sample of 10% is adequate for the generalization of the findings to the whole population if the sample size is more than 30 elements. Simple random sampling technique was used to select the actual respondents from the target population in the categories preferred that is; board of directors, directors, senior managers, finance and accounts staff. This comprises a sample size of 120 respondents to be used in data collection.



**Table 1: Sample size**

<b>Institution</b>	<b>Total</b>	<b>Multiplier</b>	<b>Sample size</b>
Kenya Broadcasting Corporation	55	.3	18
Kenya Electricity Generating Company	92	.3	31
Kenya Pipeline Company	103	.3	34
Kenya Railways Corporation	45	.3	15
National Oil Corporation of Kenya	65	.3	22
<b>Total</b>	<b>360</b>		<b>120</b>

The researcher collected primary data with the help of a questionnaire. The questionnaires were divided into five sections: the general information consisted of semi structured questions, to generally have knowledge of the background information of the respondents. The data generated by the study after fieldwork was edited, coded then entered into a computer for processing using the Statistical Package for Social Sciences (SPSS v.21.0). Descriptive and inferential statistics was used to analyze information generated from respondents. By use of percentages, frequency distributions, tables, charts, the researcher categorized the variables. Inferential statistics was used to establish whether a relationship exists in the larger population from which the sample was drawn from. This helps in making relevant generalizations whereby a Pearson correlation co-efficient was calculated to determine and test the correlation between the dependent variable and each independent variable.

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \varepsilon$$

Whereby: **Y** = Financial Performance (FP);

**X<sub>1</sub>** = Autonomy Status (AS);

**X<sub>2</sub>** = Board Effectiveness (BE);

**X<sub>3</sub>** = Government Supervision (GS);

**X<sub>4</sub>** = Regulations Overlap (RO); and

**B<sub>0</sub>, β<sub>1</sub>, β<sub>2</sub>, β<sub>3</sub>, β<sub>4</sub>** =Regression model coefficients

**ε** = Error Term

## Results and Discussions

The study used a sample size of 120 respondents from which 111 filled in and returned the questionnaires making a response rate of 92.5 %. According to Mugenda and Mugenda, (2005), a response rate below 40% is unreliable, a response rate of 40%-50% is poor, a response rate of 50%-60% is acceptable for analysis and reporting, a response rate of 60%-70% is good and a response rate of 70%-80% is very good while response of over 80% is excellent. This response rate of 111 out of 120 respondents was excellent, very satisfactory and representative to make conclusions for the study.

## Descriptive Statistics

### Autonomy Status

Table 1 depicts the results of the level at which respondents agreed with statements on the influence of Autonomy Status and financial performance in the state funded entities in Kenya. A scale of 1-5 was

used. Where; 1= Strongly Agree; 2 = Agree; 3 = Neutral; 4 = Disagree and 5 = Strongly Disagree on the continuous likert scale.

**Table 1: Autonomy Status**

	Mean	Std. Deviation
In this institution, the approach to compliance needs to be that which inspires the spirit of enterprise for increased financial performance	1.8108	.81479
The workings of the institution (state funded entity) give much less latitude for decision makers to conduct business competitively	2.2523	.86832
The top leadership in this institution cannot discharge their duties optimally due to conflict of interest	1.9009	1.33454
The directors and top management majorly serve the interest of the appointing authority and thus compromise financial performance of the institution	2.3514	.55018

From the findings, the study established that majority of the respondents strongly agreed that In this institution, the approach to compliance needs to be that which inspires the spirit of enterprise for increased financial performance as indicated with a mean of 1.8108 and a standard deviation of 0.81479, respondents however agreed that The workings of the institution (state funded entity) give much less latitude for decision makers to conduct business competitively as shown by mean of 2.2523 and a standard deviation of 0.86832.

Greater part of the respondents also strongly agreed that the top leadership in this institution cannot discharge their duties optimally due to conflict of interest as shown by a mean of 1.9009 and a standard deviation of 1.33454 and finally, majority of the respondents also agreed that the directors and top management majorly serve the interest of the appointing authority and thus compromise financial performance of the institution as shown by a mean of 2.3514 and standard deviation of 0.55018. The study results in this category were in sync with those of Kisero (2011), who found out that to run a business/enterprise, management must be accorded ample power to manage, but to run it effectively, it must be held accountable for the use of this power. This power of autonomy can boost its independence hence better performance.

### **Board Effectiveness**

The study also sought out to find out the level of agreement of the respondents with statements on board effectiveness and financial performance in the state funded entities in Kenya. A scale of 1-5 was used. Where; 1= Strongly Agree; 2 = Agree; 3 = Neutral; 4 = Disagree and 5 = Strongly Disagree on the continuous likert scale.

**Table 3: Board effectiveness**

	<b>Mean</b>	<b>Std. Deviation</b>
In order to enhance accountability and good business performance in the long term, it is a requirement that meritocracy be instilled from the top	2.2973	.85912
In developing new strong tie contacts through brokering or other contacts to explore new possibilities in product, service, or market development improves the organization performance	2.4414	.96939
Board members recognize the role which they and each of their colleagues are expected to play and have the appropriate skills and experience for that role.	2.3604	.81790
In this organization, there is no clear performance parameters for the board as well as the leadership/management	1.8378	.73287

It was established from the study results that majority of respondents agreed that in order to enhance accountability and good business performance in the long term, it is a requirement that meritocracy be instilled from the top as shown by a mean of 2.2973 and a standard deviation of 0.85912. The respondents also agreed that, in developing new strong tie contacts through brokering or other contacts to explore new possibilities in product, service, or market development improves the organization performance with a mean of 2.4414 and a standard deviation of 0.96939.

It was also noted from the study findings that, board members recognize the role which they and each of their colleagues are expected to play and have the appropriate skills and experience for that role as shown by a mean of 2.3604 and a standard deviation of 0.81790. Finally, the respondents however strongly agreed that, in state funded entity sector, there are no clear performance parameters for the board as well as the leadership/management as shown by a mean of 1.8378 and a standard deviation of 1.73287. The report by KPMG, (2014) supports the study findings by recommending that, for adequate corporate governance, the appointment of board members and top executives into state-owned enterprises must follow a clear process of transparency and meritocracy. Global Integrity, (2007) also supported the findings by highlighting that in Kenya the pressure is now on boards to live up to their responsibilities and reduce or eliminate corporate governance abuses

### **Government Supervision**

Table 3 depicts the results of the level of agreement of the respondents on statements towards government supervision and financial performance in the state funded entities in Kenya. A scale of 1-5 was used. Where; 1= Strongly Agree; 2 = Agree; 3 = Neutral; 4 = Disagree and 5 = Strongly Disagree on the continuous likert scale

**Table 3: Government Supervision**

	<b>Mean</b>	<b>Std. Deviation</b>
The organization operate within environments with elaborate supporting pieces of legislation in place as well as a high proliferation of oversight institutions	2.3964	.96558
Internal processes in the institution is outdated and ineffective in as far as identifying business risks to enable prevention or mitigation from its occurrence	2.3063	.90245
Due to the long bureaucratic processes involved in improving government processes, the controls are slow in keeping up with the fast-paced contemporary business environment	1.8649	.71968
The organization is characterized by lack of ethical precedent at the acme of leadership and reluctance of top government leaders to punish their errant cronies strips	2.3153	1.08696

From the findings, it was revealed that majority of respondents agreed that the organization operate within environments with elaborate supporting pieces of legislation in place as well as a high proliferation of oversight institutions as indicated by a mean of 2.3964 and standard deviation of 0.96558, the respondents were largely in agreement to the fact that, Internal processes in the institution is outdated and ineffective in as far as identifying business risks to enable prevention or mitigation from its occurrence as indicated by a mean of 1.8649 and standard deviation of 0.71968.

Majority of the respondents however strongly agreed that, due to the long bureaucratic processes involved in improving government processes, the controls are slow in keeping up with the fast-paced contemporary business environment as indicated by a mean of 2.5150 and a standard deviation of 0.71857. Finally, the study findings also showed that majority of the respondents agreed that the organization is characterized by lack of ethical precedent at the acme of leadership and reluctance of top government leaders to punish their errant cronies' strips as shown by a mean of 2.3153 and a standard deviation of 1.08696. These findings were supported by Global Integrity, (2007) report which argued that, internal processes in African government institutions are mostly outdated and highly ineffective in as far as identifying business risks to enable prevention or mitigation from its occurrence. Due to the long bureaucratic processes otherwise involved in improving government processes, the controls are slow in keeping up with the fast-paced contemporary business environment.

### **Regulations Overlap**

The study sought to find out the extent of agreement of the following statement on regulations overlap and financial performance in the state funded entities in Kenya. A scale of 1-5 was used. Where; 1= Strongly Agree; 2 = Agree; 3 = Neutral; 4 = Disagree and 5 = Strongly Disagree on the continuous likert scale.

**Table 4: Regulations Overlap**

	Mean	Std. Deviation
The existing regulatory framework for the state funded entities in Kenya is characterized by regulatory overlaps which inhibits financial performance	1.7838	.45538
I strongly feel that there is lack of optimal regulatory structure for parastatals in Kenya and this impacts on financial performance	2.9189	.96422
The regulator does not have adequate resources allocation so as to enable the parastatals perform optimally	2.4595	.72342
The Reforms and policy implementation is slow in the parastatal sector and this inhibits financial performance	2.5946	1.00343

It was established from the study that the respondents strongly agreed that the existing regulatory framework for the state funded entities in Kenya is characterized by regulatory overlaps which inhibits financial performance as shown by a mean of 1.7838 and a standard deviation of 0.45538; the respondents on the other hand agreed that, they strongly feel that there is lack of optimal regulatory structure for parastatal in Kenya and this impacts on financial performance as shown by a mean of 2.9189 and a standard deviation of 0.96422.

Majority of the respondents also agreed that, the regulator does not have adequate resources allocation so as to enable the parastatals perform optimally as shown by a mean of 2.4595 and a standard deviation of 0.72342. Finally, the respondents also agreed that, the Reforms and policy implementation is slow in the parastatal sector and this inhibits financial performance as shown by a mean of 2.5946 and a standard deviation of 1.00343. These findings were in sync with those of Kihara (2006) who asserted that, Parastatals in Kenya are subject to overlapping regulations. For instance, although all directors and chief executives of the Communications Commission of Kenya ("CCK") are appointees of the minister under the Kenya Communications Act, CCK is still governed by the State Corporations Act 1986 because it is a state corporation. As such, the President is empowered by the State Corporation Act to appoint the chief executives and the situation has a great influence on the performance of the institutions.

### **Financial Performance**

Table 5 established the extent of agreement of the respondents in regard to statements on the financial Performance considering the existing corporate governance mechanisms (autonomy of state funded organizations, board effectiveness, government supervision and regulations overlap) A scale of 1-5 was used. Where; 1= Not at all Satisfied; 2 = Slightly Satisfied; 3 = Some What Satisfied; 4 = Satisfied and 5 = Extremely Satisfied on the continuous likert scale.

**Table 5: Financial Performance**

	<b>Mean</b>	<b>Std. Deviation</b>
Achievement of goals	2.4955	1.08606
Net profit Margin/Surplus	2.4505	1.00669
Development Index	2.4054	.95706

According to the study results, it was established that majority respondents agreed that achievement of goals by state funded institutions was slightly satisfying as indicated by a mean 2.4955 and a standard deviation of 1.08606, the respondents also consented to the fact that Net profit Margin/Surplus was slightly satisfying as shown by a mean 2.4505 and a standard deviation of 1.00669. Lastly, the respondents asserted that the development index of state funded institutions was slightly satisfying as indicated by a mean 2.4054 and a standard deviation of 0.95706.

### **Inferential Statistics**

#### **Regression Analysis**

In this study a multiple linear regression model was implemented to identify the relationship between the four independent variables and the dependent variable which is financial performance of state funded entities in Kenya. The study applied the statistical package for social sciences (SPSS) to code, enter and compute the measurements of the multiple regressions for the study. The finding of the study is as shown in table 6 below.

**Table 6: Model Summary**

<b>Model</b>	<b>R</b>	<b>R Square</b>	<b>Adjusted R Square</b>	<b>Std. Error of the Estimate</b>
1	.899 <sup>a</sup>	.808	.800	.19649

a. Predictors: (Constant), Autonomy Status (AS), Government Supervision (GS) , Regulations Overlap (RO), and Board Effectiveness (BE)

It is evident from the study results as portrayed in Table 7: Model Summary that all the four independent variables (Autonomy Status (AS), Government Supervision (GS), Regulations Overlap (RO), and Board Effectiveness (BE)) that were studied, explain only 80.8% of the on the financial performance in the state funded entities in Kenya, as represented by the R Square (R<sup>2</sup>). This implies that Autonomy Status, Government Supervision, Regulations Overlap, and Board Effectiveness as corporate governance mechanisms contribute significantly to the financial performance.

**Table 7: Analysis of Variance (ANOVA)**

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	17.179	4	4.295	111.237	.000 <sup>b</sup>
	Residual	4.093	106	.039		
	Total	21.272	110			

a. Dependent Variable: Financial Performance

b. Predictors: (Constant), Autonomy Status (AS), Government Supervision (GS), Regulations Overlap (RO), and Board Effectiveness (BE)

In an attempt to test the significance of the model, the study used ANOVA. From Table 4.12 the P-value is 0000<sup>b</sup> which is less than 0.05 thus the model is statistically significance in predicting the considered corporate governance mechanisms (Autonomy Status (AS), Government Supervision (GS), Regulations Overlap (RO), and Board Effectiveness (BE)). The F critical/tabulated at 5% level of significance is 2.46. Since F calculated (value =111.237) is greater than the F critical, this shows that the overall model is significant. The coefficients of the multiple regression models are presented in the table 8.

**Table 8: Regression Coefficients**

	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	.497	.130		3.808	.000
Regulations Overlap (RO)	.240	.065	.289	3.709	.000
Government Supervision (GS)	.174	.06	0.089	2.9	.003
Board Effectiveness (BE)	.335	.055	.551	6.068	.000
Autonomy Status (AS)	.060	.061	.077	.996	.004

a. Dependent Variable: Financial Performance

The regression model has established that considering (Autonomy Status (AS), Government Supervision (GS), Regulations Overlap (RO), and Board Effectiveness (BE)) at constant zero, venture performance is at 0.497. The generated model is therefore given by:

$$Y = 0.497 + 0.060X1 + 0.335X2 + 0.074X3 + 0.240X4 + \varepsilon$$

From the study findings, the researcher gathers that, Board Effectiveness (BE) was established to have the greatest influence on financial performance of state funded entities at 0.335 % followed by Regulations Overlap (RO) at 0.240, then Government Supervision (GS) at 0.074 and finally Autonomy Status (AS) at 0.060. This notwithstanding, all the variables were significant as their P-values were less than 0.05. At 5% level of significance and 95% level of confidence; the t statistics helps in determining the relative importance of each variable in the model. As a guide regarding useful predictors, the research determines the t values well below -0.05 or above +0.05.

The study results explicitly show this significance on each of the variable considered that is: (Constant), (Autonomy Status (AS), Government Supervision (GS), Regulations Overlap (RO), and Board Effectiveness (BE)) will always be significant with regards to venture performance since the multiple regression analysis ( $\beta_0 = 0.497$  and  $p = 0.000$ ,  $\beta_1 = 0.060$  and  $p = 0.004$ ,  $\beta_2 = 0.335$  and  $p = 0.000$ ,  $\beta_3 = 0.074$  and  $p = 0.003$  and finally  $\beta_4 = 0.240$  and  $p = 0.000$ ).

## **Conclusions**

From the findings of the study, it was concluded that:

As to whether autonomy of state funded organizations affect financial performance, the study concludes that, autonomy status of state funded organizations is always a significant factor towards financial performance in the state funded entities in Kenya at  $\beta_1 = 0.060$  and  $p = 0.004$  and being the least influential variable in the model. The study results however show a positive relationship meaning an improvement in autonomy status will always lead to an improved in the financial performance of state funded organizations in Kenya.

Analysis of the effects of Board effectiveness on financial performance of the state funded entities in Kenya revealed that, Board effectiveness is also a significant corporate governance element towards financial performance of the state funded entities in Kenya. The study findings showed that Board effectiveness will always a significant corporate governance element towards financial performance of the state funded entities in Kenya at  $\beta_2 = 0.335$  and  $p = 0.004$  and being the most influential variable in the model. The study findings also show a positive relationship meaning a more effective board will always lead to an increase in financial performance of the state funded entities in Kenya.

Analysis of the third objective which was to investigate the relationship between Government supervision and financial performance in the state owned entities in Kenya revealed that, Government supervision will always a significant factor for financial performance in the state owned entities in Kenya at  $\beta_3 = 0.074$  and  $p = 0.003$  and being the second least influential variable in the model. The study results also show a positive relationship between Government supervision and financial performance of the state owned entities in Kenya meaning improved and proactive government supervision will always lead to an increase in financial performance of the state owned entities in Kenya

The fourth and the last objective of the study were to determine the influence of Regulations overlap on financial performance of the state owned entities in Kenya. On this objective the study duly concludes that, Regulations overlap will always be a significant factor for financial performance in the state owned entities in Kenya at  $\beta_4 = 0.240$  and  $p = 0.000$  and being the second most influential variable in the model. The study results also showed a positive relationship between Regulations overlap and the financial performance in the state owned entities in Kenya meaning an improved effort in addressing the regulations overlap will always lead to an increase in the financial performance in the state owned entities in Kenya

Finally, holding all the other factors constant, the financial performance in the state owned entities in Kenya was tested against key corporate governance elements measured by their significance and established that in deed the corporate governance elements (Autonomy Status (AS), Government Supervision (GS), Regulations Overlap (RO), and Board Effectiveness (BE)) contributed to 80.8% of the variation of financial performance in the state owned entities in Kenya as explained by adjusted  $R^2$  of 0.808.



## Recommendations

The study recommends the following;

Judging by the outcome of the study, the researcher proposes that, the state funded entities should be made aware of the fact that by adopting governance standards, they not only improve their image but also their performance. This will ensure the well-being of all stake holders and better flow of funds. Instead there is need of meaningful governance regulations to enhance autonomy in the state funded entities in Kenya

It is also recommended that, there is also a need to streamline the overlapping regulations in order to give parastatals some autonomy, which would enable them to meet targets set under the performance contracts they have entered into with the government. Reforming the regulations relating to appointment in order to ensure that directors are appointed transparently and on the basis of their competence, rather than closeness to public officials, is necessary because incompetent directors are unlikely to achieve the targets set under the performance contracts.

The study recommends that, the board of directors of the state funded entities to be accountable to parliament. Parliament can also reinforce accountability, as parliament would demand accountability and require ministers to adopt corporate governance practices. Having such an arrangement in place would facilitate the appointment of qualified persons, and in turn, enhance the performance of the boards by raising the standard of care expected from directors.

Considering the study results, the researcher proposes that since firms with good governance practices have performed better, it should be left to the regulators, corporate governance thinkers and policy makers in deciding the range of optimum levels for these variables (Corporate Governance facets) for the effective governance of the firms which is good for all stakeholders. The board of directors should uphold more superior accountability standards for improved corporate governance

## Suggestions for Further Study

Due to the ever changing nature of business environment in general, a similar study should be conducted after a period of time in the parastatal sector in order to investigate whether there are any areas of unique factors.

The study findings also revealed that the corporate governance facets considered in the study that is; Autonomy Status, Government Supervision, Regulations Overlap, and Board Effectiveness only accounted for 80.8% of the variation in financial performance as explained by adjusted R<sup>2</sup> of 0.808. Meaning other corporate governance elements not tested in the current study should be considered for future research.

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