

**EFFECT OF CORPORATE GOVERNANCE ON FINANCIAL PERFORMANCE OF  
SAVINGS AND CREDIT COOPERATIVE SOCIETIES IN KENYA**

**BY**

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**MASTER OF BUSINESS ADMINISTRATION (CORPORATE MANAGEMENT)**

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**A DISSERTATION SUBMITTED IN PARTIAL FULFILLMENT OF THE  
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BUSINESS AND PUBLIC MANAGEMENT AT KCA UNIVERSITY**

**OCTOBER, 2016**

**DECLARATION**

I declare that this dissertation is my original work and has not been previously published or submitted elsewhere for award of a degree. I also declare that this contains no material written or published by other people except where due reference is made and author duly acknowledged.

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## ABSTRACT

The enactment of the SACCO Act of 2008 established SASRA as an entity or state authority that regulates the Cooperative societies in Kenya, with the regulation covering deposit taking and to some extent non-deposit taking SACCOs. The enactment of SASRA regulation requires SACCOs to improve on corporate governance. This study was thus carried out with the aim of understanding the effects of corporate governance on the performance of SACCOs in post SASRA era. Specifically the study focused on analyzing the effect of board of director's tenure, board diversity and meeting frequency on the financial performance of SACCOs. The study used cross-sectional study design and had a target population of 49 that comprised of deposit talking SACCOs in Kenya. The researcher collected data from the respondents through secondary data and analyzed the same through SPSS. Data was analyzed using SPSS with regression analysis, ANOVA, and co-efficient of determination ( $R^2$ ) used to interpret the results. The study revealed that corporate governance practices affect the financial performance of SACCOs. This was by 28.4% and 28.6% without control and with control variable respectively. Specifically without control variables the results showed (0.061), 0.002, 0.017, 0.026, (0.004) and 0.018, indicate the effect of professional expertise, gender diversity, average tenure of directors, frequency of meetings and age of board members. On the inclusion of control variable the results indicated that gender and director tenure was significant while the rest of the variables were not significant. The study concludes that social heterogeneity and director tenure affect financial performance of SACCOs. Thus the study recommends the need effective implementation of gender diversity and director on tenure regulations.

**Keywords:** SACCOs, Performance, Corporate Governance, Meetings Frequency, Directors Tenure, Board Diversity

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## **DEDICATION**

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## TERMS AND DEFINITIONS

**Board Diversity:** defined as real or perceived differences among people in language, race, ethnicity, sex, age, physical and mental ability, sexual orientation, religion, work and family status, weight and appearance, and other identity-based attributes that affect their interactions and relationships (Bell, 2012).

**Board Tenure:** Refers to the duration within which board members serve (Faleye et al., 2012)

**Corporate Governance:** It's a term often used to describe the way an organization is managed; monitored and held accountable (Agumba, 2008).

**Financial performance:** It is the measure of financial health of an organization measured over a period of time in a given period of time and in comparison to similar firms in the same industry in sector (Weche, 2004)

**Firm Size:** This refers to the value of assets that an organization owns in an industry (Ragama, 2006).

**Gender Diversity:** The representation of Women and Men in Board (Das et al., 2011)

**Professional Expertise:** Refers to the specialized skill or knowledge that is possessed by a person in a particular area of specialization (Faleye et al., 2012)

## **ABBREVIATION AND ACRONYMS**

**ACCOSCA** – African Confederation of Cooperatives, Savings and Credit Associations

**ANOVA** - Analysis of Variance

**BOSA** – Back office Services Activities

**CEO** - Chief Executive Officer.

**FOSA** – Front office service Activities

**GDP** – Gross Domestic Product

**KUSCCO** – Kenya Union of Saving and Credit Cooperatives

**ICURN** – International Credit Union of Regulators Network

**ICPSK** - Institute of Certified Public Secretaries of Kenya

**ICPAK** – Institute of Certified Public Accountants of Kenya

**NIM** – Net Interest Margin

**ROE** – Return on Equity

**ROA** – Return on Assets

**SACCO** – Savings and Credit Cooperative

**SASRA** – Sacco Societies Regulatory Authority

**SPSS** – Statistical Packages for Social Sciences

**WOCCU** – World Council of Cooperative Union

## **CHAPTER ONE**

### **INTRODUCTION**

#### **1.1 Background of the Study**

Cooperative financial institutions (CFIs) or savings and credit cooperatives or other terms that differ across regions of the world are among the poorly understood entities in most countries that comprise the existing institutional base for financial intermediation (Cuevas & Fisher, 2006). These institutions' are member owned whose core business is to encourage thrift and easy access to credit to their members. Members pull resources together in form of savings, and the SACCO uses the mobilized savings to extend small credit facilities to them (Manyara, 2006). They are user-owned financial cooperatives that offer savings, credit and other financial services to their members. Co-operatives, like other private sector enterprises, have not remained untouched by the recent corporate governance scandals. SACCO governance is the system in which SACCOs are led, enabled and its leadership held accountable for the actions taken in a bid to manage the SACCOs in the interests of all members (Accosca, 2012).

Cooperatives are member based associations which own by business firms or are employee based. For example, milk farmers may come together and establish a dairy or customer based associations in a village or urban areas and join forces to establish their own Cooperatives. They may also want to establish their own bank or Insurance companies to act as a financial mutual (Thonsen & Conyon, 2012). One of the principal challenges facing SACCOs and other Cooperative entities is the establishment and Institutionalization of proper governance models that can improve their effective and efficient business operations. Good Corporate Governance can improve the performance of institutions and helps in ensuring its long term survival in the face of stiff competition. Corporate Governance is the system by which an institution is directed, controlled and held accountable. It is the manner in which power is exercised in the stewardship

of its assets and resources to increase and sustain shareholders value and to satisfy the needs and interest of all stakeholders (Ademba, 2012). One of the principal challenges which SACCOs face is that of establishing proper governance systems (Branch & Baker, 1998). Good governance can improve the performance of a SACCO and help in its long term survival (Thomsen, 2008). The issue of corporate governance has become of increasing interest to SACCOs as it is considered to be one of the weakest areas in the industry (CSFI, 2008). According to Labie & Mersland (2011), there are several reasons for governance to be at the forefront of SACCO debate of which among the major ones are firstly, the tremendous growth in service providers of various types translates to a greater number of clients and assets, as well as more elaborate structure to manage.

Secondly, there have been numerous institutional and legal changes with SACCOs building more and more elaborate networks and turning into shareholder-owned regulated financial institutions. Thirdly, institutions are evolving, from focusing mostly on a single product (usually credit) to becoming more complete banking institutions that provide not only credit, but also savings and sometimes other types of financial services such as money transfers, remittances, payment systems and insurance, therefore reinforcing the risks assumed by the SACCOs. Fourthly, the behaviour of public authorities towards SACCOs is also changing since their original neglect is being replaced by more proactive policies that create regulatory and supervisory frameworks supposed to favour sound development of the industry (such as the recent introduction of SACCO Societies Regulatory Authority- SASRA in Kenya).

### ***1.1.1 Corporate Governance in SACCOs***

Governance in a Sacco Society context can be defined as generally involving a set of relationships between the Sacco Society on the one hand, and its management, board of directors, members and other stakeholders on the other hand. Corporate governance in a Sacco Society therefore means the structure through which the objectives of the Sacco Society are set outlined and the means of attaining those objectives, monitoring and how performance is determined (Agumba, 2008). Cooperative Societies operates in an environment surrounded by communities who depend on them for jobs, tax, revenues, quality services and products. Co-operatives also operate in an environment which is characterized by political interest, market existence, cultures, values, technology and regulations. The relationships which directors of co-operatives have with their members are very different one from that of the board with its shareholders. As a result, Co-operative directors have full understanding and knowledge about the operations of the Co-operative movement, what is called information asymmetry (Agumba, 2008).

In Kenya, the Annual General Meeting is the supreme organ which authorizes Operationalization of budgets, it also gives SACCOs borrowing powers and decides on whom to be in the management committees, the Executive Committee and other committees of the board (Odhiambo,2012). During Annual General Meetings, transparent elections for Executive Committee members are held under the supervision of the Ministry of Industry and small enterprises formerly Ministry of Co-operatives and Marketing officials. A well thought out governance structures, like in Kenya's case has to a greater extent made Co-operatives relatively stronger in terms of decision making, members' participation and general performance in funds mobilization, service delivery and products provision scope.

The SACCO management is currently empowered to make and effect investments, bond expansion, marketing strategies, and corporate social responsibilities. (Odhiambo,2012). According to WOCCU (2011), there are several reasons for proper corporate governance to be at the forefront of Sacco's debate of which amongst the major ones are; firstly, the tremendous growth in services provided by the SACCOs that translates to a greater number of assets and clients as well as the elaborate structures to be managed. Secondly, there have been numerous institutional and legal challenges as SACCOs continue to build more and more elaborate networks making them to be transformed into shareholders owned regulated institutions. Thirdly, these institutions have been evolving, focusing not only on credit, but becoming more like banking institutions receiving deposits from general public through the FOSA and BOSA operations. They are also opening their bonds and engaging the member of public instead of doing business with their members only.

SACCOs are engaged in money transactions like fund transfers, remittances, payments and Insurance services. Fourthly, the behavior of the public and other institutions towards SACCOs is also changing rapidly since their previous underperformance coupled with poor management practices is being replaced with more stringent policies created by the regulatory and supervisory frameworks that favor the development of SACCOs, such as the introduction of Sacco Society Regulatory Authority- SASRA in Kenya (Odhiambo, 2012). Kenya is regarded as the leading country in Africa in the Cooperative movement according to the report by Accosca, (2010). There are approximately 15,000 registered SACCOs which contributes about 13.1% to GDP with membership of about 6.5million. The movement has however faced various challenges ranging from corruption, embezzlement of funds, political interference, lack of proper conducive business structures and operating framework. Due to these reasons, the government undertook

reforms in the SACCO industry through the establishment of SACCO Society bill 2008 (Kuscco Ltd, 2012). In this regard, the provisions of the *Sacco Societies Act (Cap 490B)* and the Regulations made thereunder, as read with the *Cooperative Societies Act (Cap 490)* and the Rules made thereunder provide an elaborate governance structure for a deposit-taking Sacco Society, together with the interplay between the various statutory governance institutions. From the supremacy of the members through the general meeting as limited by the law, the delegation of governance through an elected board of directors, the constitution and composition of various board committees, to the separation of the oversight roles of the board of directors and management, the important role that good corporate governance ought to play in the stability of a deposit-taking Sacco Society cannot be over-emphasized (SASRA, 2015). To help in the implementation of corporate governance structures in SACCOs , SASRA developed guideline on good governance practices with the main objective of ensuring that the members of Sacco Societies, the Board of Directors, individual directors, management and other stakeholders clearly understand their various roles, duties and obligations within the confines of the law and good practices(SASRA, 2015).

### ***1.1.3 Concept of Financial Performance***

Financial performance is the measure of financial health of an organization measured over a period of time and in comparison to similar firms in the same industry in sector. There are many different ways to measure financial performance, and these measures may take either subjective or objective. The objective measurement of financial performance of an organization usually includes reference to the financial statement and includes the use of the following ratios; return on assets (ROA), Return on Equity (ROE) and Net Interest Margin (NIM) are the major ones

(Weche, 2004). ROA is a major ratio that indicates the profitability of a business entity. ROA refers to the ratio of income to total assets while net interest margin (NIM) is a measure of the difference between the interest income generated by banks/SACCOs and the amount of interest paid out to their lenders, relative to the amount of their assets. The return of equity (ROE) is a financial ratio that refers to how much profit a company earned compared to the total amount of shareholders equity in invested. Subjective financial performance measurement has also been used to measure the financial performance of organizations through collection of primary data from employees, managers, shareholders, investors among others. Subjective financial performance was used in this study to measure the financial performance of SACCOs.

#### ***1.1.4 Sacco Regulatory Authority***

Sacco Regulation Authority was established in 2008 to regulate the operation of deposit taking Sacco's in Kenya. Most of the Sacco's that with national networks had accumulated huge savings from their members and were opening branches throughout the country at the same time operating front office services, Odhiambo, (2012). They were also venturing into risky businesses like real estate development, purchase of other businesses through acquisition and mergers, joint ventures which resulted to collapse of Sacco's in the long run. Hence SASRA was established through legislation by the government to regulate deposit taking Sacco's, (Odhiambo, 2012). SASRA is a member of International credit Union of Regulators Network (ICURN) and its roles falls within a wide scope of ongoing reform process in the financial sector with dual objectives to protect the interest of Sacco members and ensure public confidence in Sacco's; spur Kenya's growth through mobilization of savings; set standard guidelines on governance issues audited on the same lines as other corporate institutions in collaboration with ICPSK; maintain financial stability in the sector; promote technical capacity of Sacco's through

efficient management information systems through development of technical guidelines and training of key stakeholders; approval of list of qualified and experienced auditors to audit Sacco's in collaboration with ICPAK, maintenance of Key capital adequacy levels and investment guidelines; development and approve business plans and feasibility studies; Loan portfolio management and provisioning; liquidity management, control and monitoring procedures; fit and proper test to be filled and duly completed by directors and Senior Management of deposit taking Sacco's in Kenya,(Ademba, 2012). Most of these Sacco's were provisionally licensed in the year 2010 and were to be fully licensed in the year 2015. SASRA was to monitor their progress even after licensing to make sure that the above guidelines were maintained. Two Sacco's had their licenses revoked in the year 2015 due to non compliance related to regulation issues, (Kuscco, 2015).

## **1.2 Statement of the Problem**

The effectiveness of internal corporate mechanisms of SACCOs, for example boards and management composition and operations is subject to debate. This issue is particularly relevant due to the establishment of boards amongst SACCOs in Kenya and their involvement in new and risky businesses like deposit taking through Front Office Service Activities (FOSAs), opening of common bonds, investments and other related services. Kenya's corporate practices are predominantly derived from the British practices and are heavily borrowed by the Cooperative Act on their governance structures. In the international field of research, Bencht et al's (2006) found out that institution-initiated governance improvement can lead to improved firms performance. The research examined market perceived benefits instead of realized benefits of engagement.

Sacco's operates in all sector of the economy hence they play a major role in production and service delivery. The general objective of Sacco's is to promote the economic interest of its members in accordance with cooperative values and principles. The post independence era saw rapid rise in the number of Sacco's in Kenya. In 1963, there were about 465 Sacco's in Kenya, Kuscco (2015). The number of Sacco's rose rapidly to about 12,869 Sacco's in the year 2014. However, in the era of liberalization the structural adjustment programs led to the transformation of Sacco's business model. These institutions were not prepared to compete with private firms like banks which led to high levels of competition. Structural and corporate governance factors coupled with liberalization led to collapse of a number of Sacco's. This led to most Sacco's diversifying their operations including deposit taking from public and investing in real estate.

The enactment of the SACCO Act of 2008 established SASRA as a legal authority to regulate the sector in Kenya, with the regulation covering both deposit taking and to some extent non-deposit taking SACCOs, more specifically at operational level. Due to collapse of a number of Sacco's and liquidity challenges faced by these organizations, a regulation was introduced to help safeguard member's savings. SASRA regulations require SACCOS' to reconstitute their boards, improve on corporate governance and upgrade staff competence in order to improve profitability. Study by Wanyoike (2013) was carried out in Kenya to establish the effect of compliance to SASRA regulations on the performance of SACCOs. The study found out that the regulation has had a positive effect on performance of SACCOs. However, it felt short of understanding the degree to which corporate governance variable had impacted on financial performance of SACCOs.

Okwe (2011) and Ndiwalana (2014) carried out studies in Uganda on the effect of corporate governance on financial performance of SACCOs. However, the studies focused on

board composition and board meetings and were carried out in Uganda where SACCO's regulation framework is still weak unlike in Kenya. Locally, Wambua (2011) and Nyaga (2014) carried out a study on the effects of Corporate Governance on Sacco's financial performance in Kenya mainly focusing on the Deposit taking SACCOs. Nevertheless, these studies used secondary and primary data, and only focused on selected counties. Besides, the aforementioned studies have only focused on board diversity. Thus it was evident that there exists limited studies that have focused on all deposit taking Sacco's in Kenya using of only secondary data after the full implementation of SASRA regulations in 2015 and on emerging issues on corporate governance practices, hence this study will analyze the effect of specific emerging corporate governance variables (meeting frequency, board diversity and tenure of director) on performance of deposit taking SACCOs in Kenya.

### **1.3 Objectives of the Study**

#### ***1.3.1 General Objectives***

The objective of this study was to investigate the effect of Corporate Governance on the financial performance of SACCOs in Kenya.

#### ***1.3.2 Specific Objectives***

The specific objectives of the study were as follows:

- i) To assess the effect of directors' tenure on the financial performance of SACCOs in Kenya.
- ii) To determine the effect of the board meetings frequencies on the financial performance of SACCOs in Kenya.
- iii) To evaluate the effect of board diversity on the financial performance of SACCOs in Kenya.

- iv) To evaluate the effect of age of board members on financial performance of SACCOs in Kenya
- v) To assess the effect of board members professional expertise on financial performance of SACCOs in Kenya.
- vi) To determine the control effect of firm size on financial performance of SACCOs in Kenya.

#### **1.4 Research Questions**

In order to attain the study objectives, this research was guided by the following research questions:

- i) What is the effect of directors' tenure on the financial performance of SACCOs in Kenya?
- ii) What is the effect of the frequency of board meetings on the financial performance of SACCOs in Kenya?
- iii) What is the effect of gender diversity on the financial performance of SACCOs in Kenya?
- iv) What is the effect of age of board members on financial performance of SACCOs in Kenya?
- v) What is the effect of board members professional expertise on financial performance of SACCOs in Kenya?
- vi) What is the control effect of firm size on financial performance of SACCOs in Kenya?

#### **1.5 Significance of the Study**

This research is essential to various entities as outlined below. The key parties who will find the research to be particularly helpful are outlined: The study will help these parties to identify various aspects of corporate governance that have implications on the financial performance of their organizations. They will also identify the impediments that hinder the efficiency and

effectiveness of SACCO operations, thereby impacting financial performance negatively. This study will provide policymakers and legislators with useful insights into the dynamics of the cooperative movement. This will help them to craft policy and laws that will be beneficial to the advancement of cooperatives. Scholars and researchers who are interested in carrying out studies on cooperatives will find the findings of this study beneficial to their literature review efforts.

### **1.6 The Scope of the Study**

The study focused on the relationship between corporate governance and financial performance among the different SACCOs in Kenya. Specifically, the study concentrated on aspects of internal co-operative governance, i.e. The frequency of board meetings, the length of directors' tenure, and board diversity. The study used data from 49 deposit SACCOs that are in Kenya, and from different regions. These SACCOS were selected because of their implementation of SASRA regulations and subsequent renewals of their license each and every year. The study utilized only secondary data which was collected from SACCO offices country wide.

## **CHAPTER TWO**

### **LITERATURE REVIEW**

#### **2.1 Introduction**

This chapter focused on the review of literature by the researcher on the effect of corporate governance on financial performance of SACCOs in Kenya. It includes the theoretical review, empirical review, theoretical framework, and Operationalization of variables.

#### **2.2 Theoretical Review**

Theoretical review gives the meaning in terms of specific theories of a discipline. It assumes both knowledge and acceptance of the theories that depends on it by creating hypothetical construct. The study was based on the following theories: The agency theory, stewardship and resource dependency theory.

##### ***2.2.1 Agency Theory***

According to Jensen et al. (1994), agency theory is based on REEM (Resourceful-Evaluative-Maximizing-Model). The model used in Modern Corporation is determined by the corporation size and complexity as well as the need for external capital. Agency theory is manifested in situations that deal with conflict of interest such as production, innovation, and managerial labor. Assumed autonomy and self-interests create the problems within agency relationships such as the association between principals and employees. In such a situation, employees are the agents that are hired to serve the principal's interests. As applied to corporate governance, the principal uses ownership and control to ensure that his 'agents'; which are company directors serve the principals' interests instead of personal interests.

To avoid losing returns as a result of executives' self-interest, principals accept certain agency costs such as offering incentives or monitoring executive conduct to constrain the agents' opportunism. Particularly, to constrain agents' self-interest, principals employ strategies such as board diversity, board independence, director tenure, and audit committee among others. Saccos are governed by board of directors elected by members and in turn, the directors employ top management to implement strategies put in place by the board. This model is not unique to other firms and experiences conflict of interest, Agumba, (2008). Therefore, the agency theory will be used to test the impact of board diversity, frequency of board meeting and direct tenure on performance of SACCOs in Kenya.

### ***2.2.2 Stewardship Theory***

Stewardship Theory holds that there is no conflict of interest between shareholders and management and that stewards utility function is maximized when protecting and maximizing shareholders wealth. In this theory, governance is essentially to facilitate mechanism and structures that can effectively align the interest of Managers and shareholders, Donaldson & Davis (1993). Stewardship theory emphasizes on goal convergence between management and shareholders and stresses on importance of autonomous action by management that are aimed at maximizing returns for the shareholders and minimizing cost of monitoring and controlling behavior, Davis, Schoolman & Donaldson (1997). According to Daly et al (2003), in order to protect reputation as a decision maker, the Manager is motivated to operate the firm to maximize financial performance and shareholders wealth. Fama, (1970) argued that executives and directors manage their careers in order to be perceived as effective stewards of their respective firms.

According to stewardship theory, there are situational and psychological factors that predispose an individual to become a steward. Situational factors refer to work culture that is an all inclusive involvement oriented management system and a governance structure that gives authority and discretion to management. Psychological factors are motivational, disposition to identify with objectives of the firm, commitment to firms values and leadership skills, Davis et al (1997). The theory suggest that financial performance of firms and shareholders wealth can be maximized by minimizing the agency cost as suggested in line with the main objectives of this study.

### ***2.2.3 Resource Dependency Theory***

The resource dependency theory focuses on the role of board diversity in attracting critical and vital resources to an organization through their network in the external environment, Hillman, Cannella & Paetzold, (2000). According to Johnson et al (1996), resource dependency theory provides focus on appointment of representatives of independent organizations as a means of gaining access to resources critical to firm's success. To acquire critical resources, firms through directors and management create links with external environment. Directors are capable of bringing to the firm specific expertise or connection to a resource such as finance or supplies.

Thus, resource dependence role of directors suggests that board composition will have an impact on stakeholders of the firm and hence increase the potential of securing the critical resource,

Hillman, Cannells & Harris, (2002). For example, greater diversity within the board may provide an array of expertise which in turn could result in better decision making. Board diversity may exist in age, tenure, gender, functional backgrounds, professional experience and education, Coffey & Wang (1998) as well as in outside representation, Forbes & Milliken (1999)

and in a number of boards in which such director's serves. From an institutional theory perspective, boards may take on certain characteristics due to societal or business norms and pressures. Firms may follow such norms in an effort to create legitimacy with stakeholders, Pfeffer & Salancik, (1978). For example, factors such as societal and institutional pressures to increase diversity on boards, Elgart, (1983), Sign, (2005), have added legitimacy to organizations with greater gender diversity, Milliken & Martins, (1996). Previous research finds the provision of these important resources by the board significantly related to firms performance which is one of the objectives of the study- the effect of board diversity on Sacco's performance.

## **2.3 Empirical Review**

A review of studies that have been carried out on the study objectives has been presented in the section below based on the study objectives.

### ***2.3.1 Relationship between Board of Directors' Tenures and Firm Performance***

Board tenure refers to a policy formulated to ensure that the board is promoting the interest of a firm's shareholders effectively. Tenures entail the duration that directors should serve in a board, election procedures, removal of directors and performance expectations. Many organizations do not have a maximum term that directors should serve, although some specify a maximum of either three or four terms; each lasting three years and, therefore, totaling to nine or twelve years (Ragama, 2006). Longer tenure of directors is a source of reputation and valuable organizational knowledge; which can lead to better decision-making and easy access to resources (Pfeffer & Salancik, 1978). Vance (1983) also contends that forcing directors into early retirement results in a waste of knowledge and skills, experience, and organizational resources. Furthermore,

extended tenure is linked with more financial disclosures and fewer hostile-takeover bids (Kosnik, 1987; Donoher, Reed, & Storrud-Barnes, 2007).

Additionally, Buchanan (1974) asserts that long-tenured directors are likely to distribute resources appropriately thereby ensuring the realization of company goals. Similarly, Fischer & Pollock (2004) advance that an extended tenure enables company directors to acquire expertise because of familiarity with a firm's processes. Kor & Sundaramurthy (2009) also contend that longer tenure allows directors to develop knowledge of an organization's past commitments, strategic resources and capabilities. By exploiting such knowledge, the board can propose environmental goals and activities independent of the management. Furthermore, directors with such knowledge are likely to have been exposed to the firm's environmental challenges and opportunities thereby enhancing their ability to pursue appropriate environmental agenda. However, Villian (2012) established that there is a negative link between directors' tenure and an organization's financial performance.

### ***2.3.2 Relationship between Frequency of Board Meetings and Firm Performance***

These meetings refer to the assembly of shareholders with statutory limits and powers to make decisions about company goals and activities. Notably the decisions made at Annual General Meetings binds all members including those that were absent from such meetings. As such, assuming that the assembly of members is the highest organ of governance, efforts should be made to ensure effective participation and representation. Participation will be considered not only in its quantitative aspects, but also from the qualitative contribution made to the discussions, deliberations and decision-making. Effective participation requires various preparations such as shareholders formation, information sharing and individual motivation (Godfrey, 2002).

Furthermore, good corporate governance practices require board of directors to meet regularly to discuss the challenges facing a firm and formulate appropriate strategies. Particularly, the board of directors' meetings must not be held for less than six times in the fiscal year. A few past studies have highlighted the role of board of directors' meetings on the performance of a firm. While a firm may lack management experience, the expected benefits of frequent meetings outweigh the costs. Accordingly, frequency of board meetings is positively linked to firm performance. However some scholars argue that there is no impact of board meetings' frequency on firm performance. For example, El Mehdi (2007) established that the frequency of board meetings has no significant relation with economic performance in 24 Tunisian firms listed from 2000 to 2005. Therefore, El Mehdi (2007) concluded that financial performance of a firm; which is closely linked to the quality of the daily management of a firm, is unaffected by the frequency of board meetings.

Similarly, Ntim & Osei (2011) in a study of a sample size of 169 corporations in South Africa concluded that board meetings' frequency is negatively associated with corporate performance. Another research that was conducted on Malaysia's 328 public listed companies using data of 2003 to 2007 demonstrates that many board meetings signify low performance in an organization (Amram, 2011). Okpan (2015) also studied the link between frequency of board meetings and performance of a firm using a sample size of 79 listed companies in Nigerian Stock Exchange Market since 2010 to 2012. The study found out that the association between the frequency of board meetings and firm performance is negative. Generally, there is no consensus in the empirical literature on the subject. Besides, the literature is overly concentrated in a few developed countries particularly in Europe and North America; which have similar institutional context (Conger et al., 1998; Yermack, 1996; Carcello et al, 2002).

For example, using a sample of 307 US firms listed in the 1990-1994 period, Vafeas (2009) established a negative relationship between the number of board meetings and firm performance. Notably, Vafeas (2009) found out that operating performance improves significantly after a year of higher board activity. This suggests that while meeting regularly can enable directors to monitor firm performance and make better decisions, the benefits of such intense monitoring should reflect in future performance even when the numbers of meetings reduce. On the contrary, Karamanou and Vafeas (2005) established a positive relation between board meeting frequency and a firm's financial performance. Therefore, further research is required to test the hypothesis that frequency of board meetings is linked positively to a firm's financial performance.

### ***2.3.3 Relationship between Gender Diversity and Performance of Firms***

Gender diversity and firm performance has remained under consideration by a number of prominent researchers for last few decades. In particular, various studies have been conducted in the third world to determine the impact of gender on firm performance. Consequently, the outcomes of this findings are mixed. In fact, there is no consensus on whether gender affects firm performance negatively or positively. According to Farrell & Hersch (2005), women were mostly employed in successful firms. Besides, announcement that women were appointed to the board documented insignificant abnormal returns. However, Smith et. al. (2006) argues that the demand for women directors was not based on performance. In fact, appointment of women to the board was response to internal and external calls for diversity. Accordingly, Smith et. al. (2006) established that the presence of women in top management usually has a positive effect on firm performance.

In particular, presence of women in the board selected by members of staff affects the firm positively. In fact, providing women with influential position makes the performance of the firm to vary from none to positive in relation. Consequently, positive effects of women in top management strongly depend on the qualifications of female top managers. Additionally, female directors have a significant impact on board inputs and firm (Adams and Ferreira, 2009). As a result, gender diverse boards are more efficient to governance and monitoring because women are regular and punctual in comparison to men. However, increasing women ratio in the board does not guarantee good performance in firms. Hussein and Kiwia (2009) investigated the relationship between female board members and firm performance for a panel of 250 US firms.

On one hand, the outcomes had no positive and significant relationship between performance measures of ROA, Tobin's Q ratio, gender influence and gender mix. Moreover, board diversity shows negative or neutral outcomes with different performance measure such as cumulative stock returns (Dobbin and Jung, 2011). Consequently, investors are biased and avoid to investing in firms with female directors which results in a decline in stock prices. As a result, gender diversity plays an important role in determining firm performance. However, the role of gender diversity in the boardroom has been ignored in developing countries where gender discrimination is common. Gender diversity is an emerging issue in the corporate world (Julizaermaa & Sori, 2012). Omar and Davidson (2001) observe that the number of women pursuing managerial careers is on the increase. However, women representation on the board of directors is generally low. Carter et al. (2002) contend that board diversity results in board independence because women are more inquisitive than men directors. In addition, women directors introduce new ideas and skills and contribute positively to the firm (Singh and Vinnicombe, 2003).

Furthermore, presence of women in firm's board may enhance and improve the firm's performance (Campbell & Mínguez-Vera, 2008; Julizaermaa & Sori, 2012). Agrawal and Knoeber (2000) also posit that presence of women directors in the board intensifies collaborative skills. Moreover, Adams and Ferreira (2009) established a significant relation between gender diversity and return on assets. The relationship is consistent with the univariate test result that higher gender diversity in top management is positively associated with higher levels of firm performance. Ararat et al. also found a positive relationship between gender diversity and firm performance. Similarly, Lu'ckerath-Rovers (2011) established that firms with women directors perform better than those without women on their boards. However, Yasser (2012) observed that firms in Pakistan do not have a significant relationship between board and gender diversity. Consequently, firm performance is measured as an economic value added. Furthermore, the Malaysian government established a goal of 30 percent female board membership (Azmi & Barrett, 2014). However, Abdullah et al. (2012) argue that women have a distinct managerial style in Malaysian firms. As a result, there is a positive and significant relationship between the presence of women directors and Malaysian firms' performance as measured by ROA.

### ***2.3.3 Relationship between Age of Board Members and Firm Performance***

Additionally, age diversity of directors is an essential attribute of a board. If the directors of a board are of the same age group, the leadership and the decision-making styles of the board might be biased towards a particular age segment of the market. This is because the directors may have similar information and experiences. Appointing directors from different age groups will help the board to tap information from directors who understand better the need and the sensitivity of the stakeholders in their age group. The board should reflect society which is, in

reality, heterogeneous in composition. In particular, Carter et al. (2003) established that younger boards are gender sensitive in comparison to older boards. Therefore, younger directors are more flexible as opposed to old directors who are more rigid. According to Higgs (2003), non-executive directors from the UK are notably drawn from a narrow pool. Consequently, most directors in the UK are 60 years old and above white males. Similarly, most directors in Australian firms' fall within the 51-70 age band while few directors (1.98%) are below 40 years old. Therefore, diversity is not pronounced with respect to ethnicity and age among boards of most Australian firms (Kang et al. 2007). Additionally, age is a significant demographic variable while addressing board diversity. According to Kang et al. (2007), there is an active promotion of age diversity in boards to encourage the different perspectives of different age groups and as an integral part of succession plan. In particular, one of the recommendations of the European Commission is age diversity in most firms. The commission argues that age diversity improves the boards overall level of knowledge (COM 2010).

However, various findings on the relationship between age diversity and corporate performance are inconsistent. While some studies show positive effects of age diversity on performance, others do not reveal either significant or negative effects,(Kilduff et al. 2000; Mahadeo et al. 2012; Bunderson and Sutcliffe 2002; Zimmerman 2008; Murray 1989; Milliken and Martins 1996). Accordingly, the inconclusive findings indicate that previous research has omitted the interactions among different aspects of diversity. In fact, in a review of theories and methodologies of top management team diversity, Nielsen (2010) highlights that the distinction of diversity as variety, separation, and disparity (Harrison and Klein 2007) needs to be applied to future research. Furthermore, researchers have conducted investigations on the effects of directors' age on firm performance. According to Child (1974) and Vroom & Pahl (1971), older

managers are more likely to avoid risky decisions. However, Hambrick and Mason (1984) argue that young managers are likely to undertake risky strategies. As a result, firms with young managers will experience higher growth than their counterparts with older managers. Japanese firms show significant negative relationship between age and firm performance (Nakano & Nguyen, 2011). However, after using firm size as a controlling variable they found that the age is more significant, consistent with the notion that older directors are more likely to retain their positions in strongly performing firms. Using a sample of 169 Indonesian firms, Darmadi (2011) established that the proportion of young members is positively related to firm performance, also, the study provided evidence that young people in the boardrooms are associated with improved firm performance.

Letting et al. (2012) examined the relationship between Board diversity and financial performance of firms 40 firms listed in the Nairobi Stock Exchange. The study employed the Ordinary Least Squares (OLS) regression. As such, the study established that there is a significant positive relationship between ROA and age of director's members. Mahadeo et al. (2012) examined the key elements of board diversity and its influence on financial performance in an emerging economy; they found a positive association between age different age groups on board and company performance. In addition, Akpan and Amran (2014) examined the relationship between board characteristics and company performance measured by turnover. The study established that there is no relationship between board age and firm performance. Similarly, Eulerich et al. (2014) conducted investigated the relationship between diversity within management boards and firm performance in German. The research demonstrated negative effects on the relationship between age and firm performance because of large age differences which may alleviate decision-making processes.

#### ***2.3.4 Relationship between Professional Expertise and Firm Performance***

Research on the effect of professional background and expertise of directors on firm performance is limited to date (Aldamen et al. 2012, Gray, Harymawan and Nowland 2016, Christensen, Kent and Stewart 2010). Gray and Nowland (2015) give a summary of the Australian research which focused on particular types of expertise. Gray and Nowland (2015) also provide the first classification of director expertise, which involves eleven distinct groups. These groups include academics, bankers, accountants, consultants, engineers, doctors, executives, other CEOs, lawyers, politicians and scientists.

Gray and Nowland (2015) established that diversity of director expertise had no overall effect on organizational performance. However, a negative correlation was found between non-business expertise and company performance. Various studies on the subject identify background and professional expertise the reasons as reasons for director appointments. For example, Agrawal and Knoeber (2001) suggest that individuals with backgrounds in politics are likely to be hired as directors for companies with significant government contracts while companies in which environmental regulation is higher tend to hire qualified lawyers. Fich (2005) also established that companies tend to appoint CEOs with a successful record of past performance as directors. However, Güner, Malmendier and Tate (2008) found out that financial expertise of directors does not necessarily benefit shareholders.

#### ***2.3.5 Relationship between Firm Size and Firm Performance***

The performance of firms is determined by various factors such as customer satisfaction, market growth and sales, and financial results among other factors (Dvir et al., 1993). According to Ritab et al. (2004) return on assets (ROA) also play an important role on the performance of

firms. In fact, Ritab et al. (2004) posit that ROA is usually a measure of a firm's profitability. As such, ROA is key performance indicator in various organisations (Yammessri and Loth, 2004). In addition, the performance of firms is determined by the growth of organisations. In particular, firm growth plays an important role in determining the lifecycle of an organisation. Notably, firms must maintain a competitive advantage over rivals through continuous growth (Kazmi, 2002; Johnson et al., 2008). While growth is not the primary objective of new entrants, absence of growth indicates organizational failure especially in mature companies (Coad, 2009; Honjo and Haranda, 2006).

The size of organizations also determines the performance of firms. For example, Chi (2004) states that while the profitability in large organization is high, small companies lack the capacity to compete with big firms. For instance, the capital value of large companies enables the organizations to obtain loans easily from banks and other lending institutions. Besides, the credit value of big corporations enables the firms to obtain loans at lower rates because they have minimal chances of becoming bankrupt. Notably, Penrose (1959) hypothesized that firm size is an indicator of resource capacity and organizational capability. According to Penrose (1959), larger firms have more resources to facilitate the realization of organizational goals than smaller firms. Accordingly, Wu (2006) argued that as a result of greater resource availability, larger firms have higher competitive capabilities than the smaller organisations. However, Rauch et al. (2009) found out an inverse relationship between firm size and performance. Yi & Tzu (2005) also argue that firm size does not determine the performance of organisations. Similarly, Gibrat (1931) identified the growth rate of a firm as independent of its size. This finding is referred to as the "Law of Proportionate Effect".

According to Bhattacharyya (2009), this law holds that growth is unrelated to the firm size. Therefore, large and small firms have equal chances of attaining high growth rates. In fact, ineffective management in big firms may result in low performance while effective management in small firms may result in firm growth, and high profits (Gedajlovic and Shapiro, 1998). Therefore, although the size of firms may determine the success of companies, it is not guaranteed that big companies will perform better than small firms. According to Vijayakumar & Tamizhselvan (2010), various researchers have conducted studies on the relationship between firm size and performance. Hall (1987) and Barret et al., (2010) established an inverse relationship between diversification and firm performance. As search more research is required to determine the relationship between diversification and firm performance. In addition, Lee (2009) employed the fixed effect dynamic panel data model to examine over 7000 US publicly-held firms. The study revealed that firm size plays an important role in explaining profitability.

Besides, Ozgulbas et al. (2006) established that the effect of firm size on performance of companies operating in Istanbul Stock Exchange. The studies established that the performance of big scale firms is higher compared to small scale firms. Similarly, Jonsson (2007) established that bigger firms have higher profitability as compared to smaller firms. Furthermore, Amaton & Burson (2007) examined the linear and cubic form of the size-profit relationship in the financial services sector. Consequently, the research detected the presence of cubic relationship between return on assets and firm size. In addition, a study conducted in American manufacturing firms by Becker et al. (2010) reveals that there is a negative and statistically significant relation between the total assets, total sales and number of employees of the firms and their profitability. According to Velnampy & Nimalathan (2010), a positive relationship exists between firm size

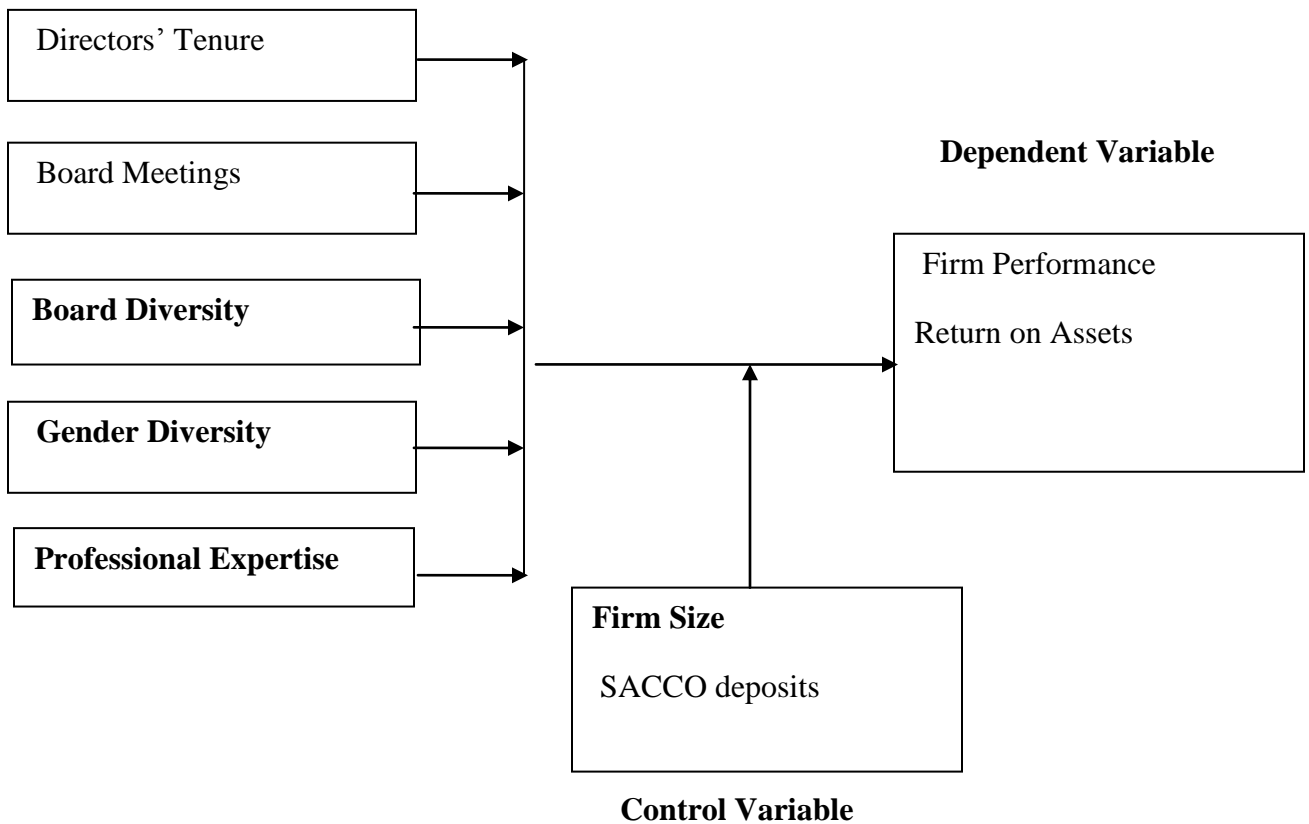
and profitability in Commercial Bank. However, there is no relationship between firm size and profitability in commercial banks.

## 2.4 Conceptual Framework

A conceptual framework is a logical illustration of the interrelationships between the study variables as envisaged by the research. The conceptual framework for this study is elucidated in figure 1 below.

**FIGURE 1**  
**Conceptual Framework**

### Independent Variable



*Source: Author (2016)*

## 2.5 Operationalization of Variables

The Operationalization of variables table (table 1) shows the various theoretical statements through which the research used to measure the study constructs. Secondary data was used to operationalize the data.

**TABLE 1**  
**Operationalization of Variables**

<b>Variables</b>	<b>Indicator</b>	<b>Measurement</b>	<b>Type of Analysis</b>
Directors' Tenure	Years as a director	Nominal ordinal	Descriptive
Board Meetings	Number of board meeting in a year	Nominal ordinal	Descriptive
Board Diversity	Annual reports, delegate report and budgets	Nominal ordinal	Descriptive
Gender Diversity	Number of men and women in board	Nominal Ordinal	Descriptive
Professional Expertise	Professional Experience of directors	Nominal Ordinal	Descriptive
Firm Size	SACCOs deposits	Continuous Variable	Descriptive
Finance Performance	Return on assets (ROA)	Ration	Descriptive

*Source: Author (2016)*

## **CHAPTER THREE**

### **RESEARCH METHODOLOGY**

#### **3.1 Introduction**

This chapter provides a description of procedures to be used in carrying out the study. It describes the research design, target population, sample size and sampling procedures, data collection and procedures, as well as the other data processing and presentation methods/data analysis techniques.

#### **3.2 Research Design**

This study adopted a descriptive cross-sectional analysis because the data involved several SACCOs. A descriptive study attempts to describe study unit (SACCOs in this case) often by defining unit characteristics through the collection of data on research variables or their interaction (Obwatho, 2011). This study chose a descriptive cross sectional as its design because it seeks of lack of additional complete data over the previous years (2014-2012) to evaluate the effects of corporate governance practices on financial performance of SACCOs in Kenya. Complete data was only available for the year 2015.

#### **3.3 Target Population**

A report by SASRA (2015) indicated that there are a total of 176 deposit taking SACCOs in Kenya and about 49 Sacco's secondary data met the criterion and fitted into our objectives of the study. Most of the Saccos had not fully complied with all reporting requirement to fit into this study.

### **3.4 Sampling and Sampling Technique**

The sample size of the study was 49 compliant SACCOs which are fully compliant with the latest SASRA reporting requirements. The study used purposive sampling to select the participating SACCOs. This was used to select the firms that have met the reporting standards.

### **3.5 Data Collection Procedure**

The study used secondary data. The data was collected from annual reports, human resource reports, financial statements, delegates' reports, board minutes and other reports available in the SACCOs (SACCOs Reports, 2015). The age, gender and expertise variable of the study was sourced from inception report that every SACCOs files to SASRA whenever a board member is elected. The frequency of meetings was collected from board minutes and yearly delegate's reports on meetings of board members. The tenure of directors was collected from report filed with by every SACCO at SASRA compliant offices. Return on assets was sourced from Sacco's financial statements for each year.

### **3.6 Data Analysis and Presentation**

The study used a multiple linear regression model to determine the relationship between the dependent and the independent variables. The dependent variable in the study was the financial performance while the independent variables were directors' tenure, board diversity (gender, age and expertise) and meeting frequency. The regression model for this study was thus:

$$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \beta_6 X_6$$

Where:

**Y**= the dependent Variable (i.e. the financial performance of Sacco's)

**$\alpha$**  = Constant term for the independent variable

**$\beta_1$** = Co-efficient of **X<sub>1</sub>** Variable

**X<sub>1</sub>** = Directors Tenure

**$\beta_2$**  = Co-efficient of **X<sub>2</sub>** Variable

**X<sub>2</sub>** = Frequency of Board Meetings

**$\beta_3$**  = Co-efficient of **X<sub>3</sub>** Variable

**X<sub>3</sub>**= Age

**$\beta_4$**  = Co-efficient of **X<sub>4</sub>** Variable

**X<sub>4</sub>**= Gender

**B<sub>5</sub>** = Co-efficient of **X<sub>5</sub>** Variable

**X<sub>5</sub>** = Expertise

**B<sub>6</sub>** = Co-efficient of **X<sub>6</sub>** Variable

**X<sub>6</sub>**= Size of SACCO deposits as a control variable

## **CHAPTER FOUR**

### **FINDINGS AND DISCUSSION**

#### **4.1 Introduction**

The chapter presents data analysis and interpretation of findings to establish the effect of corporate governance on the financial performance of SACCOs in Kenya.

#### **4.2 Descriptive Statistics**

This study carried out the following descriptive statistics; mean, variance, standard deviation, minimum and maximum values. The descriptive statistics for the independent variables indicates that firms under this study had a mean of 2 for gender indicating that most Sacco's have not met the gender rule in board. On Age of directors the average age of directors was between 46-55 years indicating that most directors are not youths. On professional expertise the mean was 2 indicating that most of director had background in financial management. On board meeting frequency the mean was 2 indicating that most SACCOs had between 14-15 meetings in a year. On director tenure the findings show a mean of 2 indicating that majority of SACCOs are compliant with the SASRA regulations. Return on assets for Sacco's had a mean of 0.03269 indicating low returns among most SACCOs. SACCO deposits on the other hand has a mean of 0.939 indicating that most SACCOs are still small.

**TABLE 1**  
**Descriptive Statistics**

<b>Variables</b>	<b>Min</b>	<b>Max</b>	<b>Mean</b>	<b>Standard Deviation</b>
Return on Assets	(0.1401)	0.1363	0.03269	0.0412
Sacco Deposits	0.00	4.39	0.6179	0.939
Gender Diversity	1	4	2	1.056
Age of Board Members	2	4	3	0.666
Professional Expertise	1	3	2	0.662
Board Meetings	1	3	2	0.694
Director Tenure	1	3	2	0.621

*Source: Author (2016)*

### 4.3 Normality Tests

Test of Assumption was carried out before regression analysis, specifically normality tests was done with results presented.

**TABLE 2**  
**Normality Tests**

<b>Tests of Normality</b>						
	<b>Kolmogorov-Smirnov<sup>a</sup></b>			<b>Shapiro-Wilk</b>		
	<b>Statistic</b>	<b>df</b>	<b>Sig.</b>	<b>Statistic</b>	<b>df</b>	<b>Sig.</b>
Return on assets	.198	49	.000	.850	49	.061
EXPAT	.277	49	0.00	.783	49	.054
GENDER	.211	49	.00024	.861	49	.088
Average Tenure of Board Directors	.315	49	.0010	.769	49	.0167
Average age of board members	.287	49	.023	.793	49	.0110
MEET	.319	49	.003	.477	49	.114
DEPSIZE	.263	49	.045	.674	49	.232

a. Lilliefors Significance Correction

*Source: Author (2016)*

Normality tests were carried out for the study with the possibility of kolmogorov-smirnov test and Shapiro-Wilk test. However, Shapiro-wilk test was used in the study since the sample size of the study was less than 2000. The study results indicate that all the variables were normal

except age of board members and director's tenure. This was indicated by p-value less than 0.05. A possible explanation could be linked to the cluster of data around one response thus minimizing the normality of data. The data was generally normal and thereby allowing for further regression analysis.

### **Tests for Multicollinearity**

Test for multi collinearity for the independent variables was carried out through variance inflation factor with results presented below. From the table below it was evident that variance inflation factor were all less than 4. This indicates the absence of multi-collinearity thereby allowing for further regression.

**TABLE 3**

**Tests for Multicollinearity**

<b>Variables</b>	<b>VIF</b>
Gender Diversity	1.16
Professional Experience	1.03
Age Diversity	1.49
Board Tenure	1.23
Frequency of meetings	1.08
SACCO Deposits	2.43

*Source: Author (2016)*

**4.4 Board Diversity**

The study sought to establish the effect of board diversity on financial performance of SACCOs. Board diversity included the following (Age, Gender and Expertise of board members). The results are presented in the section below.

**4.4.1 Gender Diversity of Boards**

The study sought to analyze the gender diversity in boards of deposit taking SACCOs. The results of distribution of respondents based on gender were as presented in Table 5 below. From the results it was established that 59%(29) of boards had less than a third women, 16%(8) had more than a third of women in boards, 12%(6) had no women and 12%(6) had a third women in boards. This study implies that Sacco's boards are yet to meet the gender requirement rule of third women in boards. These results affirm the findings of IOD (2014) and KIM (2012) that found out that women representation in boards in financial institutions is low (at 14%) when compared to other sectors.

**TABLE 4**

**Board Gender Composition**

<b>Gender</b>	<b>Frequency</b>	<b>Percent</b>
Less than a third Women in Board	29	59
More than a Third of Women in Board	8	16
No Women in Board	6	12
A third of Women in Board	6	12
Total	49	100

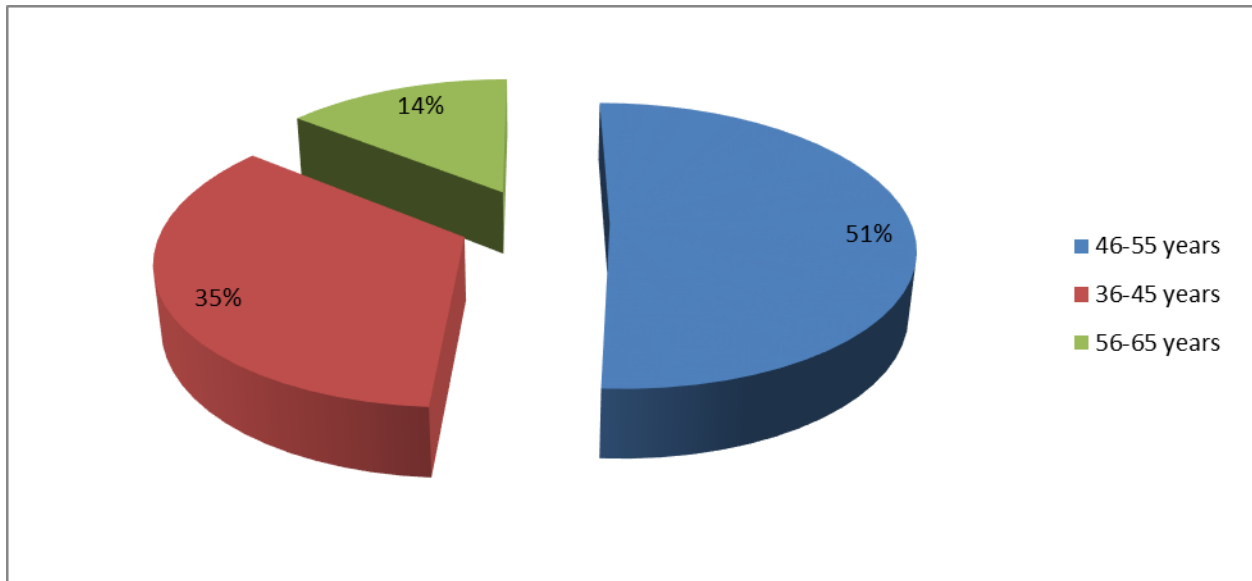
*Source: Delegates and Financial Report (2015)*

**4.4.2 Average Age of Directors'**

The study sought to analyze the age of board members. Figure 4.2 show the results of distribution by age brackets. Majority of the respondents (51%) were between age 46-55 years while 35% were between 36-45 years and 14% were between 56-65 years. These findings indicate that SACCO board members have no youths in its board. This was confirmed by Akpan and Amran (2014) who found out that youth are relatively few in board members due to other board diversity variables such as expertise and experience that tends to leave the youths out.

**FIGURE 2**

**Average Age of Board Members**



*Source: Delegates and Financial Report (2015)*

#### ***4.4.3 Professional Expertise of Board Members***

The study sought to find out the expertise of the board members in deposit taking SACCOs. The result of the study indicated that majority of board members had expertise in financial management (44.9%), organizational service area (40.8%) and legal and human resource (14.3%). These results attest to the crucial expertise that financial institutions need. These results are similar to the findings of johl et al, (2015) and Minton et al, (2012) who concluded that financial management expertise is the key expertise for financial institutions.

**TABLE 5**

**Professional Expertise of Board Members**

<b>Expertise</b>	<b>Frequency</b>	<b>Percent</b>
Financial Management	22	44.9
Organizational Service Area	20	40.8
Legal+ Human Resource	7	14.3
<b>Total</b>	<b>49</b>	<b>100</b>

*Source: Delegates and Financial Report (2015)*

**4.5 Board of Director's Tenure**

The study was out to find the average tenure of directors at the deposit taking SACCOs. The results are presented below.

**4.5.1 Average tenure of directors**

Table 7 shows the average tenure of directors in the study. Majority of board members had tenure between 4-6 years at 49% while 27% and 25% had tenure above 6 years and 1-3 years. These results indicate compliancy with the SASRA regulations which prescribes the maximum years for directorship to two terms of 3 years each. These findings are similar to the results of Wairimu (2014) and Nyaga (2014).

**TABLE 6**

**Average Tenure of Directors**

<b>Tenure of Board Directors</b>	<b>Frequency</b>	<b>Percent</b>
4-6 years	24	49
Above 6 Years	13	27
1-3 Years	12	25
<b>Total</b>	<b>49</b>	<b>100</b>

*Source: Delegates and Financial Report (2015)*

## 4.6 Board Meetings

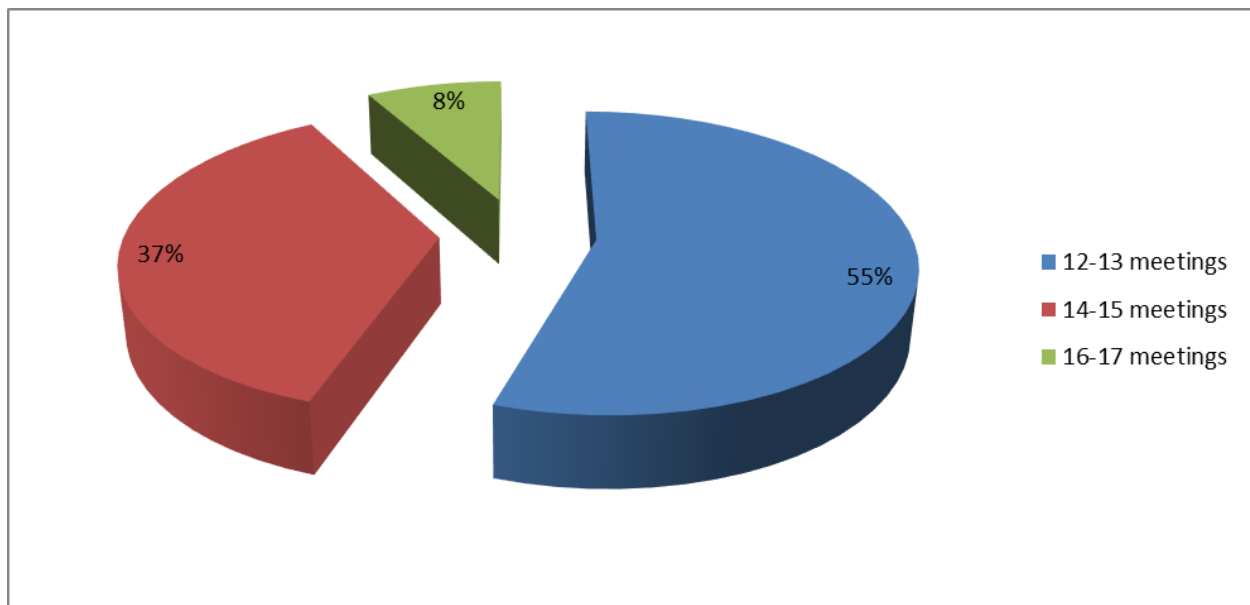
The study sought to establish the frequency of meeting among the deposit taking SACCOs in Kenya. The results are presented below.

### 4.6.1 Number of board meetings

Figure 3 below shows the average number of board meetings held by deposit taking SACCOs board per year. These firms indicate existence of general trend in number of board meeting in private sector where according to Guo(2011) is equivalent to approximately one meetings a month.

**FIGURE 3**

**Number of Board Meetings**



*Source: Delegates and Financial Report (2015)*

#### **4.7 Relationship between the Corporate Governance Practices and Financial Performance of SACCOs.**

An analysis was performed on the relationship between the corporate governance and financial performance of SACCOs. The study assumed a linear relationship between the corporate governance practices and financial performance of SACCOs and used the Ordinary Least Square (OLS) method of estimation in seeking the line of best fit. Before the regression analysis, the data was subjected to assumptions of regression analysis, with no violation being observed. Model was tested with or without the control variables. The linear relationship was modeled into equation (1) below.

The estimators in equation (1) were defined as;  $\alpha_i$  was the estimate of the intercept showing the financial performance in the absence of the factors and  $\varepsilon$  was the error term related with this equation,  $\beta_1$  was the beta coefficient of director's tenure ( $X_1$ ),  $\beta_2$  was the beta coefficient of frequency of meetings ( $X_2$ ),  $\beta_3$  was the beta coefficient of board diversity ( $X_3$ ) and  $\beta_4$  was the beta coefficient of firm size ( $X_4$ ). Following a linear regression analysis, the ANOVA output is presented for both with or without control variables. The results are presented below. From this table, the model was significant (p-value = 0.023) at 0.05 level in explaining the linear relationship between the factors and financial performance.

**TABLE 7****Model fitting without control variable**

<b>Model</b>		<b>Sum of Squares</b>	<b>df</b>	<b>Mean Square</b>	<b>F</b>	<b>Sig.</b>
1	Regression	0.023	6	0.004	2.781	0.023b
	Residual	0.058	42	0.001		
	Total	0.082	48			
a Dependent Variable: Return on assets						
b Predictors: (Constant), Number of Board Members , MEET, EXPAT, Average age of board members, GENDER, Average Tenure of Board Directors						

*Source: Author (2016)*

**TABLE 8****Model Fitting with Control Variable**

<b>Model</b>		<b>Sum of Squares</b>	<b>df</b>	<b>Mean Square</b>	<b>F</b>	<b>Sig.</b>
1	Regression	0.023	7	0.003	2.347	0.041b
	Residual	0.058	41	0.001		
	Total	0.082	48			
a Dependent Variable: Return on assets						
b Predictors: (Constant), DEPSIZE, MEET, Average Tenure of Board Directors , GENDER, EXPAT, Average age of board members, Number of Board Members						

*Source: Author (2016)*

From the table 8 and 9 above, the model was significant (p-value = 0.041 and 0.023) at 0.05 level in explaining the linear relationship between the factors and financial performance. This means that the model is appropriate for use in interpreting the effect of corporate governance practices on financial performance of SACCOs. In Table 8, the model had a coefficient of determination ( $R^2$ ) = 0.284, indicating that 28% of the variation in financial performance was explained by the model leaving 72% of the variations in financial performance as unexplained. Model one therefore provided a weak fit. The study results indicated a similarity in R results with or without control variable. This could be attributed to what Taracha (2014) says is because most SACCOs have nearly the same range of deposits, with no big difference.

**TABLE 9**

**Model Summary without Control Variable**

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.533a	0.284	0.182	0.03729
a Predictors: (Constant), Number of Board Members , MEET, EXPAT, Average age of board members, GENDER, Average Tenure of Board Directors				

*Source: Author (2016)*

**TABLE 10**

**Model Summary with Control Variable**

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.535a	0.286	0.164	0.0377
a Predictors: (Constant), DEPSIZE, MEET, Average Tenure of Board Directors , GENDER, EXPAT, Average age of board members, Number of Board Members				

*Source: Author (2016)*

R squared has a value of 0.284 and 0.286 which shows that approximately 28% is explained by the independent variables included in the model. Adjusted R<sup>2</sup> of 0.182 and 0.164 variation in the dependent variable (ROA) is explained by the independent variables (board diversity, director tenure and frequency of meetings). Adjusted R<sup>2</sup> indicates the true behavior of the dependent variable that varies in accordance with the independent variable. Whereas a very low percentage of the changes in the dependent variable can be attributed to the independent variable, however this model is significant. This is because it has an F-statistic value of 2.31 and 2.71 which are relatively greater than one thereby proving the model significance.

**TABLE 11**

**Regression Co-efficient without Control Variable**

	<b>Unstandardized Coefficients</b>	<b>Std. Error</b>	<b>Standardized Coefficients</b>	<b>t</b>	<b>Sig.</b>
(Constant)	(0.061)	0.05		-1.225	0.227
EXPAT	0.002	0.008	0.036	0.267	0.791
GENDER	0.017	0.007	0.38	2.645	0.011
Average Tenure of Board Directors	0.026	0.008	0.449	3.04	0.004
MEET	(0.004)	0.008	(0.068)	-0.517	0.608
Average age of board members	0.018	0.009	0.291	2.046	0.047
a Dependent Variable: Return on assets					

**Source: Author (2016)**

An interpretation of the coefficients in Table 12 shows expertise had a non-significant coefficient with p-value = 0.791, frequency of meetings had a non-significant coefficient with p-value = 0.608. This implies that expertise, frequency of meeting do not affect the performance of SACCOs, Gender, director tenure and average age of board members had a significant values of 0.011, 0.004 and 0.047 respectively. This implies that gender, director tenure and average age affects firm (Sacco’s) performance.

From the estimated regression equation;

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 \dots\dots\dots(i)$$

The coefficients analysis gives  $\beta_3$  and  $\beta_4$  are 0.476 and (0.234). Where  $\beta_0$  is the constant = (0.061),  $\beta_1 = 0.002$ ,  $\beta_2 = 0.017$ ,  $\beta_3 = 0.026$ ,  $\beta_4 = (0.004)$  frequency of meeting and  $\beta_5 = 0.018$  consecutively. The fitted regression equation of the model becomes;

$$Y = (0.061) + 0.002 X_1 + 0.017 X_2 + 0.026 X_3 - 0.004 X_4 + 0.018 X_5 \dots\dots\dots(ii)$$

It is evident from the above regression model that if all factors were to be held constant then a unit change in corporate governance factors result in a (0.061) change in financial performance of SACCOs. Table 12 presents the regression results of the study without control variable. The regression coefficient of Gender was positive and significant in predicting the financial performance of Nigerian firms. This implies that women representation in board offers SACCOs good resource mix that in turn improves the financial performance of SACCOs. The findings of the study are consistent with the results of Okwee(2011) and Kamonjo(2012). The regression coefficient of average tenure of directors was positive and significant in predicting the financial performance of deposit taking SACCOs in Kenya. This result could be attributed to what Westphal & Khanna, (2003) say about longer tenure increasing director independence as it offers some insulation against social isolation for objecting to a course of action preferred by management and other directors. This results are similar to the findings of Villier and Nakier(2011) who established that longer tenure tends to improve the performance of firms.

The regression coefficient of expertise and frequency of board members appeared to be insignificant in the study. This could be influenced by level of expertise and quality of meetings which was not tested in this study. This is because Byrd and Mizruchi (2005) argues that for expertise to be significant to financial performance of firms it must be based on years of experience and not only educational qualification. Concerning the meetings Makhoulf et al (2011) argues that quality of meeting is key determinant to the financial performance of firms rather than number of meetings. The regression coefficient of average age of board members and performance appeared to be significant in the study. This could be influenced by the reason that age allows board members to gain experience in their profession and thus can easily contribute effectively to improve the financial performance of SACCOs. These findings are consistent to

the findings of Dagsson, & Larsson (2011) who found that age improves financial performance of firms. From the findings of the study it was noted that corporate governance practices causes a change in financial performance by 28% with other variables not included in the study causing a change of financial performance by 72%. This significance has been established in studies by Nyaga(2014; Taracha(2014) and Dagsson, & Larsson(2011).

**TABLE 12**

**Regression Co-efficient with Control Variables**

	<b>Unstandardized Coefficients</b>	<b>Std. Error</b>	<b>Standardized Coefficients</b>	<b>t</b>	<b>Sig.</b>
(Constant)	-0.057	0.052		-1.114	0.272
EXPAT	0.002	0.008	0.03	0.214	0.832
GENDER	0.017	0.007	0.379	2.605	0.013
Average Tenure of Board Directors	0.026	0.009	0.453	3.023	0.004
MEET	-0.004	0.008	-0.067	-0.506	0.615
Average age of board members	0.017	0.009	0.285	1.964	0.056
DEPSIZE	0.002	0.006	0.045	0.312	0.756
a Dependent Variable: Return on assets					

*Source: Author (2016)*

An interpretation of the coefficients in Table 13 shows expertise had a non-significant coefficient with p-value = 0.832, frequency of meetings had a non-significant coefficient with p-value = (0.004). This implies that expertise and frequency of meetings affect performance of firms. Gender and director tenure had significant values of 0.017 and 0.0026 respectively. Thereby implying gender and director tenure affect financial performance of SACCOs

From the estimated regression equation;

$$Y = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \beta_6 X_6 \dots \dots \dots (iii)$$

Where  $\beta_0$  is the constant = (0.057),  $\beta_1 = 0.002$ ,  $\beta_2 = 0.017$ ,  $\beta_3 = 0.026$ ,  $\beta_4 = (0.004)$  frequency of meeting and  $\beta_5 = 0.017$ ,  $\beta_6 = 0.002$  and consecutively. The fitted regression equation of the model becomes;

$$Y = -0.057 + 0.002 X_1 + 0.017 X_2 + 0.026 X_3 - 0.004 X_4 + 0.017 X_5 + 0.002 X_6 \dots\dots\dots (iv)$$

It is evident from the above regression model that if all factors were to be held constant then a unit change in the above Corporate governance factors would result in a (0.057) change in financial performance of SACCOs. Table 13 presents the regression results of the study with control variable. The regression coefficient of Gender was positive and significant in predicting the financial performance of Sacco in Kenya. This indicates that firm size has no control effect on the relationship between gender and Sacco's financial performance. This could possibly be attributed to the regulation that is in place by SASRA that requires all SACCOs large or small to ensure gender diversity in their boards. This result was consistent with the results of Kamonjo (2012) who established that firm size had no effect of relationship between gender and financial performance. The regression coefficient of average tenure of directors was positive and significant in predicting the financial performance of deposit taking SACCOs in Kenya. This result also indicates that firm size did not affect the relationship between director tenure and firm performance. This could possibly be attributed to the guidelines and regulations championed by SASRA for all deposit taking SACCOs. These results contradict the findings of Okwee (2011) who established that firm size affected the relationship between director tenure and performance in Uganda. A possibly explanation for this is that in Uganda director's tenure is not determined by a regulatory body as is the case in Kenya.

The regression coefficient of expertise and frequency of board members appeared to be insignificant in the study. This could be explained by the reason that SASRA has no regulation that determines the number of meetings and expertise required. Thus other factors can affect the relationship, with firm size having no effect. The regression coefficient of average age of board members and performance appeared to be significant in the study. A possible explanation for this was that firm size is a possible indicator of years of existence of SACCOs with big firm size indicating SACCOs that have been in existence for longer years thus accumulating more deposits. However, in the study most SACCOs had been in place for not more than 10 years and this is a probably indicator for relatively young age members. These findings are contrary to the findings of Dagsson, and Larsson(2011) who found that age improves financial performance of firms, notwithstanding the firm size. From the findings of the study it was noted that corporate governance practices causes a change in financial performance by 28% with other variables not included in the study causing a change of financial performance by 72%. This significance has been established in studies by Nyaga(2014; Taracha(2014) and Dagsson, and Larsson(2011).

## **CHAPTER FIVE**

### **SUMMARY OF FINDINGS, CONCLUSIONS AND RECOMMENDATIONS**

#### **5.1 Introduction**

The study sought to find the effect of corporate governance on financial performance of SACCOs in Kenya. The objective was accomplished by assessing the effect of duration of director's tenure, board diversity (age, expertise, gender) and the board meeting frequency on financial performance of SACCOs.

#### **5.2 Summary of Findings And Discussion**

The study sought to know the effect of director's tenure, frequency of board meetings and board diversity (age, expertise, gender) on financial performance of SACCOs in Kenya. The study revealed a positive and significant relationship between the directors' tenure and financial performance represented by a p-value of 0.0011. This could probably indicate the heterogeneity of board which may ensure a greater influx of new ideas for dealing with previously unforeseen threats or new opportunities thereby improving financial performance. In addition, increase in tenure can be associated with increase in experience of handling business challenges and opportunities which when tapped can enhance the financial performance. These findings are similar to Ochei (2013) and Okafor (2012) results that showed a positive relationship between director tenure and the financial performance of SACCOs. It follows that compliance with SACCO requirement on director tenure by ensuring maximum tenure of directors lead to improved performance. Concerning the frequency of the board meetings, the study revealed that there was no significant relationship between board meetings and financial performance as indicated by a p-value of 0.615.

These findings implying that boards meeting frequencies do not generate higher financial performance. This suggests that frequency of meeting may not deliberately translate to quality of meetings which can result to improved performance. These findings were contrary to the findings of Mululu (2005) who established that frequency of board meeting increases the performance of their firms. According to Mululu (2005) board effectiveness depends on the frequency of its meetings as this enhances the performance of the firm given the fact that the board is provided with more opportunity of monitoring and reviewing the performance of management. Additionally, Evans et al., (2002) and Hsu and Petchsakulwong's (2010) also revealed that boards of directors often increase the frequency of their meetings in order to find solutions to problems concerning declining firm performance. On the third objective the study sought to establish the effect of board diversity on financial performance of deposit taking SACCOs.

The study further sought to establish the effect of age, gender and professional experience on financial performance. From the regression output, results indicated a positive relationship between gender and return on assets indicated by a p-value of 0.011. By recruiting female directors, companies may accrue benefits that can impact on their financial performance through linking with their stakeholders. As discussed by Brammer et al. (2007), greater equality of representation relates to direct and indirect benefits that may potentially arise from closely reflecting the demographic characteristics of key stakeholder groups such as customers, employees and investors. Furthermore, with women in board, such appointments give SACCOs legitimacy with regard to their customers and enhances relations with stakeholders (Brammer et al. 2007).

The presence of women improves team performance, because more diverse teams may consider a greater range of perspectives and therefore reach better decisions. These better decisions then ultimately could lead to higher business value and financial performance (Singh and Vinnicombe 2004; Carter et al. 2003). This is consistent with prior studies by Erhardt, Webel and Shrader (2003), Letting, Aosa and Machuki (2012), Rovers (2010), Post and Byron (2014). The findings implies that more the number of women on a Sacco board, the better the performance of a Sacco. In view, of the fact that women are underrepresented in Sacco boards, there is need for SACCOs in Kenya to consider enlisting more women on their boards. Consistent with Mersland and Strom (2007), Terrance, Mercedes and Kimberly (2013), Khan and Vieito (2013) these findings indicate a positive relationship between gender and return on assets. This was indicated by a p-value of 0.0011 and a beta coefficient of 0.017.

From the regression output, results indicated a non-significant relationship between age and financial performance of SACCOs. This was indicated with a p-value of 0.056. These findings are similar to the results of Ararat et al., (2010) who established that age doesn't have significant impact financial performance of firms. On the same note, Nakano and Nguyen (2011) examined the effect of board age on firm performance in Japanese firms and found no significant relationship between age and financial performance of firms. The findings of the study indicated that there was no significant relationship between professional experience and financial performance of SACCOs. This was confirmed by a p-value of 0.832. This according to Klein (2008) is due to low nature of heterogeneity in most board which tend to have only directors from limited professional backgrounds.

Jensen (2003) also argues that more heterogeneous boards bring different perspectives to their monitoring and advising duties that can provide benefits to shareholders through improved resource utilization, problem solving and strategy formulation. This is echoed by Williams and O'Reilly (2008) who argues less heterogeneity means less resources to problem solving and this affects the competitiveness of organizations. This finding is supported by Das et al., (2011); Faleye et al., (2012) who established that professional experience of board members had no relationship with performance of firms. Corporate governance practices were confirmed to affect the financial performance of deposit taking SACCOs as shown by an R squared value of 28%. However, the effect of corporate governance was found to be small. A situation that Taracha (2014) attributes to the facilitation role of corporate governance practices by providing an environment that can facilitate decision making, problem solving, risk management among others. These results concur with the results of Matanda (2016) and Nyaga (2014) who established that corporate governance practices affect financial performance of SACCOs in Kenya, albeit a minimal effect.

### **5.3 Conclusion**

The study concludes that social heterogeneity (age, gender) and not occupational heterogeneity (education, expertise and experience) of boards of directors have a positive significant effect on financial performance of SACCOs. Thus the study urges for the need to place more emphasis on social heterogeneity and not occupational heterogeneity. The study results conclude that increased board diversity can impact the financial performance of the SACCO. Argrawal & Knoeber (2001) argue that board diversity, specifically women inclusion can bring along different benefits and resources when done correctly and within certain criteria.

The study also concludes that board meeting frequencies does not influence the financial performance of SACCOs in a positive fashion. The findings conclude that there is need for measures to be put in place to improve the quality of meeting and not necessarily the frequencies of meetings. These results do not support the agency theory, which suggests that corporate boards that have high number of meetings have increased capacity to pass corporate decisions that will impact on the financial performance of firms. Thus the board members, who act as agents of shareholders, may be seen as not representing the interest of shareholders in meetings as expected. The study findings indicated that the board of directors with high average tenure is also significantly related to financial performance of SACCOs. The researcher's conjecture to explain this finding is that the high tenure of BODs in a SACCO may increase synergy and a working bond between the board members thereby enabling them to forge a common front in advancement of the firm's agenda.

#### **5.4 Recommendations**

The study showed a strong positive linear relationship between the characteristics of corporate governance under study and financial performance. Therefore, the study recommends that the registered Sacco's should increase the tenure of directors and improve the diversity of their boards since this can result in improved returns to SACCOs. The study recommends the need for government and the stakeholders to improve social heterogeneity by developing policies in Sacco's especially those that promotes gender, experience and other emerging issues in corporate governance practices in the boards. The study also recommends that SACCOs should revise their rules and by laws to accommodate for reasonable tenure for directors, gender sensitivity, and experience as this may have the consequence of improving the financial performance of

SACCOs. The study recommends that SACCOs need to embrace gender mainstreaming into their boards. The study further recommends that SACCOs should not necessarily pay attention on improving age and expertise diversity in boards as these variables seem to be insignificant.

### **5.5 Recommendations for Further Research**

The study recommends the need for more studies that will focus on SACCOs in specific categories with a view to understanding the effect of emerging corporate governance practices on SACCOs in different sectors in Kenya. According to the findings of this study, it is also recommended that other variables not explained by study model be research on as only a portion of the effect is determined by the variables in the study. Variables like moral values, culture and corporate structure should be investigated to determine their effect on Sacco's financial performance.

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