INVESTIGATING CORPORATE GOVERNANCE PRACTICES IN THE KENYAN STOCK BROKERAGE INDUSTRY: OWNERSHIP STRUCTURE AND INVESTOR PROTECTION

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A DISSERTATION SUBMITTED IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE AWARD OF MASTER OF BUSINESS ADMINISTRATION (CORPORATE MANAGEMENT) IN THE SCHOOL OF BUSINESS AND PUBLIC ADMINISTRATION AT KCA UNIVERSITY

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ABSTRACT

This study is an exploratory survey on the ownership structures and investor/ client protection endeavours as components of corporate governance practise in the Kenyan stockbrokerage industry. The main purpose of the study was to bring to light, the imperative aspects of corporate governance practise by an industry recovering from its deepest decline in history, experienced during the second half of the first decade of the 21st Century. With a data from 10 out of the possible 11 firms licensed to facilitate the buying and selling of securities to the Nairobi Securities Exchange (NSE) investors, the findings of this study portrayed the industry as very volatile as a number of profound deficits in the firms' corporate governance practises were observed. The findings indicate that the ownership structure of the firms is highly concentrated with some firms having a single shareholder holding as much as 90%, mainly institutions and families. Additionally, the findings point to the lack of a clear comprehension of the tenets over and above the benefits of good corporate governance practise. It was noted that most firms comply with the corporate governance codes/ rules laid down by the Kenyan Capital Markets Authority (CMA), possibly due to the fear of the repercussions of non-compliance rather than for the ultimate benefit of the firms and the industry's different stakeholders. The mechanisms of disseminating investment related information were noted to give preference to large scale investors over the small scale investors notwithstanding the fact that if put together the small scale investors would constitute the largest block of investment holders in the firms' portfolios. The findings of this study have significant implications on the measures engineered by the Kenyan Capital Markets Authority, the Nairobi Securities Exchange and investors generally in reinforcing good corporate governance practises in the Kenyan Stockbrokerage industry.

Key Words: Corporate Governance; Ownership Structure; Investor Protection; Ownership Concentration; Agency Theory; Stakeholder Theory; Stewardship Theory; Firm Performance.

TABLE OF CONTENTS

ABSTRACT iii
ACKNOWLEDGEMENT iv
DEDICATION v
LIST OF FIGURES AND TABLES vi

CHAPTER ONE: INTRODUCTION 1
1.1 Background of the Study 1
1.2 Problem Statement 6
1.3 Objectives of Study 8
1.4 Research Questions 9
1.5 Purpose and Justification of Study 9
1.6 Limitations of Study 11
1.7 Basic Assumptions 12

CHAPTER TWO: REVIEW OF LITERATURE 13
2.1 The Theoretical Foundations of Corporate Governance 13
2.2 Ownership Structure 19
2.3 Investor Protection 21
2.4 Theorectical/ Conceptual Framework 25

CHAPTER THREE: METHODOLOGY 32
3.1 Research Design 32
3.2 Population 32
3.3 Pre-Testing, Reliability and Validity 33
3.4 Data Collection and Management 34
3.5 Data Analysis 35

CHAPTER FOUR: FINDINGS AND DISCUSSION 37
4.1 Introduction 37
4.2 Investor Protection 39
4.3 Ownership Structure 43
4.4 Findings Related To Research Questions 49
4.5 Interpretation and Discussion of Findings 53

CHAPTER FIVE: CONCLUSION AND RECOMMENDATIONS 60
5.1 The Significance of Good Corporate Governance Practice on Firm Performance..... 60
5.2 Recommendations 65
5.3 Conclusion 71

REFERENCES.. 74

Appendix I .... Questionnaire
Appendix II.. Interview Questions
Appendix III .... List of licensed Stockbrokerage Firms (2012)

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DEDICATION

I dedicate my dissertation work to my entire family and many friends. A special feeling of gratitude to my loving parents, Rufina Simiyu and Lawrence Simiyu Sifuna, whose words of encouragement and push for tenacity fuelled my drive for success. I also dedicate this dissertation to my encouraging and ever faithful friends and family members who have supported me throughout the process. I will always be grateful for all they have done.

LIST OF FIGURES AND TABLES

LIST OF FIGURES

Figure 1: Conceptual Framework 30
Figure 2: Dissemination of Investor Related Information…………………………………….. 40
Figure 3: Frequency of Information Dispersal ………………………………………………… 42
Figure 4: Frequency of Information Update …………………………………………………... 43
Figure 5: Forms of Ownership Structure in the Industry ……………………………………… 44
Figure 6: Family Ownership …………………………………………………………………... 46
Figure 7: Institutional Ownership ……………………………………………………………... 46
Figure 8: Institutional Ownership ……………………………………………………………... 48
Figure 9: Nominee Shareholding(s) …………………………………………………………… 48
Figure 10: Director Shareholding(s) …………………………………………………………... 49

LIST OF TABLES

Table 1: Percentage of Respondents who Completed the Questionnaire(S)…………………… 38
Table 2: The Firms Net Profit in the Most Recent Declared Annual Financial Results……..… 39
Table 3: Dissemination of Investor Related Information……………………………………… 40
Table 4: Frequency of Information Dispersal 41
Table 5: Frequency of Information Update 43
Table 6: Forms of Ownership Structure in the Industry 44
Table 7: Managerial Ownership 45
Table 8: Family Ownership 45
Table 9: Institutional Ownership 46
Table 10: Diverse/ Diffuse Ownership 47
Table 11: Nominee Shareholding(S) 48
Table 12: Director Shareholding... 49

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

The emergence of large corporations necessitated the separation of ownership and control of the institutions (Dean, 2001). This meant that the owners of capital (principals) who were not well equipped to manage the institutions they owned (Dalley, 2008), acquired the services of experts (agents) and gave them the responsibility of running these institutions on their (principals') behalf (Aoki, 2011; Blair and Stout, 2011). However, there are occasions when the agents seek to serve their individual selfish interests thus exhibiting conduct that diverts from the principals' motivation of wealth creation (Ongore, 2011; Ben-Ner and Ren, 2011). In serving their own personal interests, the agents do engage in clandestine activities such as insider dealings placing their own interests at the forefront instead of focusing on the actual terms of their treaty with the principals (Johnson and Ricca, 2007). In order to lower the chances of the abuse of the agent-principal relationship, the owners of capital chose from amongst themselves members to represent them in the board of directors hence the non-executive directors (Dalley, 2008; Ongore, 2011; Padilla, 2002).

The elected members of the board were supposed to safeguard the interests of the principals from the mendacious agents (Padilla, 2002) but then again it was realized that regardless of all these measures, some of the directors bestowed with the responsibilities of safeguarding the shareholders' interests got entrenched in the malfeasance bandwagon (Ongore, 2011). In other words some of the directors who join the companies to ensure that the managers meet the end of their bargain with the principals do end up piloting the abuse of the agent-

principal relationship (Padilla, 2002; Rhee, 2008). And with that, agents might end up not being accountable for their iniquitous decisions affecting the value of the company making them free to benefit from both poor and/ or good performance of the firm at the expense of the shareholders (Padilla, 2005). In investigating the inadvertent effects of insider trading, Padilla, (2005) draws attention to the works of Easterbrook (1981, p.312), Brudney (1979, p.156) and Masson and Madharan (1991, p.335) who observed that if allowed, these agents might end up employing schemes seeking to subvert the operations of the firm hence may cashing in on the swings in the value of the company stocks.

With the potential of such inconsistencies, a system of law and sound approaches by which corporations are directed and controlled (Bartlett, 2009) focusing on the internal and external corporate structures with the intention of monitoring the actions of management and directors (Cheung and Chan, 2004) and thereby mitigating agency risks stemming from devious deeds of these corporate officers (Ramly and Rashid, 2010; Oghojafor, Okolie, Okonji and Olayemi, 2010) was set up. The high profile corporate failures witnessed in the business world by companies that were once thought as pillars of global economies such as Adelphia, Enron Corporation, Global crossing and WorldCom among others necessitated the emphasis on reform of corporate governance structures worldwide (Ongore, 2011; Basu and Dimitrov, 2010). This saw the restructuring of corporate governance mechanisms globally and thus in 2004, the Organization for Economic Co-operation and Development (OECD) revised the principles of corporate governance that it had come up with in 1999 to benefit economies, corporate entities and as securities markets. The six OECD principles of corporate governance are characterized by fairness, transparency, accountability and responsibility. Additionally institutions with global reputation such as Standard and Poor's, Moody's, the Institutional Shareholder Services (ISS)

and Governance Metrics International among others also have unique methodologies of evaluating corporate governance practices of companies which could be spontaneously used as a guideline in good corporate governance practice by any company.

1.1.1 Investor Protection

In practicing good corporate governance, considering the interests rights of investors is very of great consequence. This is essential especially in the stock brokerage industry where investors are also clients of these institutions. Most research including methodology adopted by companies in corporate governance rating focus in the rights and interests of financial stakeholders. For example Standard and Poor's analysis focuses on the rights and interests of creditors and company shareholders. Therefore what about the interests of securities investors who are the clients of the stockbrokerage firms? In the Kenyan stockbrokerage industry, the clients who invest in securities through the firms are usually the first victims in case of a collapse of the firm/s. And in case this group of stakeholders loose out their investments and where compensated through the structures laid out by the market regulators, such reparation does not even meet a substantial proportion of what some investors have lost

LaPorta, Lopez-de-Silanes, Shleifer and Vishny (2000) are of the view that the investors of financial markets need some form of protection and if stronger then it might establish the fortification of investor's property rights against political intrusion. In assessing the relationship between the legal investor protection and firm's earnings management Luez, Nanda and Wysocki (2003) observed that legal systems that out rightly safeguards the rights and interests of outside investors also restrain the chances of insiders engaging in rent – seeking behavior. The study discerned a significant link connecting the quality of accounting earning disclosed to the market participants and the level of investor protection. One important factor in the practice of

corporate governance is observed by Klapper and Love (2004) that the legal system bears little significance for well governed companies. The authors analyzed data from Credit Lyonnais Securities Asia (CLSA) which ranked corporate governance practices of 495 firms within 25 emerging markets, and reached to the conclusion that a company can still improve its corporate governance practices even in absence of a strong legal system.

1.1.2 Ownership Structure

The ownership structure of corporate entities forms one of the key features of corporate governance. This is because many studies have been able to link the structure of the ownership of firms with influence within and outside the firm. For instance, in examining the relationship between ownership structure and firm performance of 2478 Indian corporate firms from 1994 to 2000, Kumar (2003), arrived to the inference that foreign shareholding doesn't have substantial bearing on the performance of firms. The author highlights that this observation is unlike observations made by earlier studies carried out in developing countries, India being one of them where foreign ownership has always been linked with high performance of firms. A similar study carried out by Demsetz and Villalonga (2001) found out that there is no statistical significant link between ownership structure and firm performance. The study investigated the relationship between ownership structure and the performance of corporation in instances where the ownership is multidimensional.

Nevertheless studies have also been able to relate ownership structure and firm performance .An assessment of relationship between ownership structures and the board of directors in the demand for external audit services on 247 Spanish and French listed companies confirms that there is a significant link between the ownership structure and the precedencies of the board of directors as well as the demand for audit Services (Desender, Crespi, Garcia-

Cestona and Aguilera, 2009). This study concluded that the features of ownership structures contribute greatly to the practice of corporate governance within firms. Similarly, a study on the effect of firm ownership structure to the performance of firms listed in Central Eastern European (CEE) equity markets clearly indicates that government owned firms outperformed firms falling under other groups of ownership. This study observed that CEE investors found it safe to invest their funds in firms where the governments were the majority shareholders especially in uncertain and underdeveloped sectors of the markets.

1.1.3 Stockbrokerage Industry in Kenya

The trading of securities began in Kenya in the 1920s as an informal set-up without any rules or regulations governing the stockbrokerage industry (Ngugi, 2003). The first stockbrokerage firm was incorporated in 1945 as Francis Drummond & Company limited, which was then followed by the establishment of the Nairobi Stock Exchange (NSE) under the Societies Act as a voluntary association (Ngugi and Njiru, 2005). At present, the Companies Act and the Capital Markets (Corporate Governance) (Market Intermediary) Regulations 2011 form the framework for corporate governance practice in Kenya. This legal framework binds the stockbrokerage industry whose mainstream firms licensed by the Capital Markets Authority are approximately 11. Despite the existence of this framework, the stockbrokerage industry has been dogged by a number of challenges that have the potential of undermining its integrity. The most prominent nuisances have been cases of perpetual collapse of stockbrokerage firms.

To be more precise, between 2007 and 2008 a good number of investors who traded in the Nairobi Securities Exchange lost their funds after Francis Thuo and Partners, Nyaga Stock brokers and Discount Securities collapsed (Mwega, 2009). By the end of February 2010, the Kenyan stockbrokerage industry had seen a total of four of its member firms collapsing with the

final one being Ngenye Kariuki (Gakeri, 2011). According to Bitok, Kiplangat, Tenai and Rono (2011), this state of affairs signified a deficiency of good corporate governance practices in the stockbrokerage industry resulting to an immense loss of investor confidence in the Kenyan securities markets. It is therefore not surprising that after losing out their investment to unscrupulous businessmen, investors start developing distrust in the securities markets as they are no longer sure of the safety of their investment anymore.

1.2 Problem Statement

In testing the perceived relationship between corporate governance and corporate reputation in three former Yugoslavian countries, Ljubojevi´c and Ljubojevi´c (2008), come to an alarming conclusion that company's do not really comprehend the fact that good corporate governance practice is key to building corporate reputation which ultimately aids the company in achieving and sustaining competitive advantage in the market place. On the same note a survey by Okpara (2010) of 198 respondents from 100 firms listed in the Nigerian stock market and equity securities found out that there is a deficiency of good corporate governance in the country.[1] Similar observations are made by Mwaura (2007) that state owned enterprises in Kenya are plagued with poor governance issues ranging from opaque board appointment processes and as a result lack of accountability, impartiality and integrity by the board. According to the author, this condition is then worsened by the inept legal framework that's not appropriate for the present-day business environment.

In Kenya, a study that sought to examine the effect of the global financial crisis on the country highlighted that a fall in share prices in the Nairobi Securities Exchange experienced in

[1] This was after the study observed that the governance practices in the country were characterized by lack of transparency and disclosure, abuse of the rights of minority shareholders, as well as the total disregard of duties by the boards of directors among others.

2009 was partly attributed to the loss of investor confidence in the markets brought about by the collapse of stockbrokerage firms (Mwega, 2010). If not enough, the study categorically brought out the fact that poor management and colossal malfeasance became the order of the day in these firms. A report by the Africa Centre for Open Governance (AfriCOG) in 2010 identifies that the Kenyan stockbrokerage industry is plagued by low transparency and generally poor governance and as a result, the collapse of the 4 stock brokerage firms in a span of 4 years resulting to the loss of investors' funds.[2] The poor corporate governance and management practices in the Kenyan stockbrokerage industry thus centres on the ability of the ownership structures of these firms to monitor executive performance through their boards of directors and the initiatives advanced by the firms in safeguarding the interests of their customers ,that is, the investors.

Therefore, unless a clear description of the ownership structure and investor protection practices of the stockbrokerage industry is depicted then the loss of investor funds due to collapse of the stockbrokerage firms might turn out not be a thing of the past. The astronomical attention attached to the need of strengthening corporate governance practices in the securities markets since early 21 century, resulted to numerous studies on corporate governance practice. However few studies have until now examined the practice of corporate governance in developing countries (Mulili and Wong, 2011) with the few undertaken in Kenya mainly focusing on state corporations (Miring'u and Muoria, 2011; Mwaura, 2007), the banking industry (Mang'unyi, 2011), public universities (Mulili and Wong, 2011) and firms listed in the Nairobi Securities Exchange (Ongore and K'Obonyo, 2011; Ongore, 2011; Ponnu and Okoth, 2009; Waweru and Riro, 2008) with little or none carried out in the stockbrokerage industry in Kenya. It is here then that this study examined the corporate governance practices in Kenyan

[2] Retrieved from; www. africog.org on, September 12, 2012

stockbrokerage industry mainly focusing on the ownership structures of these institutions as well as the protection of investors as the customers of these firms.

1.3 Objectives of the Study

(a) Main Objective

The main objective of this study was to investigate the ownership structures and investor protection practices of the stockbrokerage firms in Kenya.

(b) Specific Objective(s)

From the overall objective, the following specific objectives are derived:

i. To examine the ownership structure of the stockbrokerage firms in Kenya;

ii. To investigate the investor protection practices of the stockbrokerage firms in Kenya.

1.4 Research Questions

i. What is the ownership structure of the stockbrokerage firms in Kenya?

ii. What is the investor protection practices of the stockbrokerage firms in Kenya?

Both questions speak to the relative practise of corporate govenance in the Kenyan stockbrokerage indurstry.

1.5 Purpose and Justification of the Study

The main purpose of this study was to examine the practice of corporate governance in the stockbrokerage industry in Kenya vis-à-vis the ownership structure as well as the protection of customers as key stakeholders. This study examined the practice of cooperate governance of

the licensed stockbrokerage firms operating in the Nairobi Securities Exchange as the sole securities market in Kenya. The results of the study are of significance to:

1.5.1 The Securities Markets Investors/ the Stockbrokerage Firms Clients

Investors rely on information on the practice corporate governance in order to analyses the risks associated with their investments. For this reason, this study provides detailed information on the practice of cooperate governance by the stockbrokerage industry in Kenya giving the investors an opportunity to be able to personally gauge the abilities of these company's to safeguard and augment their investment as intermediaries in the trading of securities. Both current and potential investors will find the information the study provides relevant to the decision making process regarding their choice of the intermediary (stockbrokerage firm) to engage in investing their funds in the securities markets and the risks associated with that particular choice. This choice is at times made blindly and the repercussions of such a naïve and uninformed choice can be observed from the loss of investor funds upon the collapse of the four stockbrokerage firms between 2007 and 2010. In view of that, this study addresses both the rights of investors as Kenya stakeholders as well as the ownership and structure of the brokerage firms operating in the Nairobi Securities Exchange as the sole securities market in Kenya.

1.5.2 The Kenyan Securities Market Regulator

The Capital Markets Authority (CMA) as the market regulator in Kenya in this case is charged with the responsibility of ensuring fairness and equality in the trading of securities in the bourses falling under their jurisdictions. Among the functions that come with such a responsibility is the empowerment to: (i) license different institutions; (ii) promulgate regulations

to govern the processes and institutions under their scope; and (iii) supervise the conformity to the rules and other related statutes by the different players in the securities markets. Some of the rules that CMA has issued include the rules on corporate governance. In a nutshell, this study is of key significance to the Capital Markets Authority as the securities market regulator in Kenya as it illuminates the practice of corporate governance by stockbrokerage firms in the aforementioned two key areas. Such information is of great significance to CMA in exercising its supervising functions, promulgating regulations that fit the existent market conditions and proper licensing as well as regulatory decisions regarding the Kenyan stockbrokerage industry.

1.5.3 The Stockbrokerage Industry

Good corporate governance practice is one of the mechanisms of creating and sustaining competitive advantage in the present day business environment (Ljubojevi´c and Ljubojevi´c, 2010). With the proper comprehension of the information the covered in the study on the practice of corporate governance, individual stockbrokerage firms in Kenya might be able to effectively analyse their current governance practices and based on the analysis, come up with corporate governance policies and structures that would in turn attract investors making the organization stand out in the industry. Such information would also be important for the sustenance of the business as well as avoiding inconveniences such as penalties from the market regulator brought about by lack of adherence and /or compliance with the corporate governance rules of the securities market regulator, that is, the Capital Markets Authority.

1.5.4 Academia

This study mainly examined two components of corporate governance practice of investor protection and ownership structure. And so apart from making available concrete

information regarding the practice of corporate governance in the stockbrokerage industry in Kenya, the study has left room for further researcher on the rest of the areas of corporate governance practice in the stockbrokerage industry. The outcome of this study can also be used by the academia for further research on the enforcement of corporate governance rules and subsequent amendments to fit the needs of the current business practice in the Kenyan stockbrokerage industry.

Additionally, proper comprehending of the outcome of this study will be of great significance to the shareholders of the firms in the brokerage industry as well as the general public at large .In this sense the shareholders will become conscious of the practices of corporate governance in the firms they own, information that might have not be available for them in the actual form.

1.6 Limitations of Study

This study only covers the stockbrokerage industry in Kenya. To be specific, the practice of corporate governance by the stockbrokerage firms operating in the Nairobi Securities Exchange as the only securities market in Kenya is measured. The collection of the completed questionnaires was 4 days after initial delivery. 26 working days was allotted for data analysis. The study was therefore completed 30 days after its inception. Though the most current data is of the utmost relevant in research, the study did not restrict the selection of literature on a specific time frame.

The study did limit the target population to the company secretaries and/or legal managers of the 11 licensed stockbrokerage firms. The study notes that there might be other relevant features of the practice of corporate governance. Nevertheless, this study only focuses on the ownership structure and the protection of customers as key stakeholders in the practice of

corporate governance making other factors beyond the scope of this study. Where possible and if any, it is recommended such features of the practice of corporate governance that have not be addressed in this study, be considered in future studies.

1.7 Basic Assumptions

Issues of corporate governance are very sensitive and more so in an area such as the brokerage industry in Kenya .This is because its non-observance carries hefty penalties from the market regulators in addition to investors losing trust/ confidence in the rogue brokerage firms which can lead to collapse of business. It is therefore an assumption by the study that the brokerage firms in Kenya carry out corporate governance practices that are characterized by globally accepted features. This is from the fact that the Capital Markets Authority requires stockbrokerage firms to conform to its rules and guidelines crafted with the internationally accepted standards in mind.

Secondly with the sensitivity attached to corporate governance practice, there was a probability that participants from the brokerage firms might either answer the questions dishonestly or if not totally refuse to respond to the questionnaires or interviews. In this case the identity of the participants was not to be disclosed and furthermore, the participants were free to withdraw from the interview and/or choose not respond to any questions they were not comfortable with. This anonymity given to both the officers and the institutions they represent ensured that each of the participants responded to the questions honestly and to the best of their abilities.

CHAPTER TWO

LITERATURE REVIEW

2.1 The Theoretical Foundation of Corporate Governance

Good corporate governance and proper management go hand in hand (Duke II and Kankpang, 2012) and the realization of a vacuum in the quality corporate governance practice made the Organization For Economic Cooperation and Development (OECD) come up with the principles of corporate governance in 1999 (Chaudhury, Das and Mishra, 2011). The 1999 OECD principles then become a global benchmark for corporate governance practice (Tudor, 2006) calling out for the protection of the rights of shareholders, the equitable treatment of shareholders, the statutory recognition of the rights of different stakeholders of corporations, the disclosure of material information regarding corporation/s such as the financial position, performance and ownership structures as well as clearly spelling out the responsibilities of the board of directors of the corporation/s (Oghojafor, Olayemi, Okonji and Okolie, 2010). The 1999 principles were reviewed in 2002 taking into account the diverse developments in both OECD member and non-member countries (Malik, 2012). Upon extensively consulting with the private sector, labor, civil society and representatives from non- OECD countries, OECD eventually launched six principles of corporate governance in 2004. These principles were formulated with the main function of facilitating economies in refining their legal and institutional frameworks for corporate governance in their countries (Cheung and Chan, 2004; Kamal, 2004).

A scrutiny of the 2004 OECD principles of corporate governance along with the current practices, one pattern emerges ,that is, focus is now diverting from the traditional shareholder centred corporate governance practice to accommodate the interests of different stakeholders of corporate entities who include among others the employees, creditors, customers, suppliers and

community surrounding the corporation (Millstein, 2005). By doing so, key stakeholders such as investors in the securities markets are assured that their investments in form of capital is safeguarded against risks such as misappropriation and fraud (Cornelius, 2005). In defining corporate governance, Tirole (2005), quotes the works of Shleifer and Vishny (1997) as well as Becht, Bolton and Roell (2002) who focused their definition of corporate governance on meeting the interests of the owners of wealth, to be precise, shareholders terming the definition as narrow and goes ahead to incorporate the interests and welfares of other stakeholders in his definition of corporate governance. In principle and in practice, this definition of corporate governance embracing the interests and roles of the shareholders, the management, the board of directors and the entire community around the corporate entity has been adopted by various international bodies such as the Organization For Economic Cooperation and Development (OECD) as well as the Islamic Principles of Corporate Governance (IPCG) (Abu-Tapanjeh, 2009). When all is said and done, a proper comprehension of the foundation of corporate governance can be achieved by a review of the three main theories, that is, the agency theory, the stakeholder theory, and the stewardship theory.

2.1.1 Agency Theory

Letza and Sun (2002) trace back the origin of the agency theory to Adam Smith who in 1937 particularly isolated cases of the management of companies getting entrenched into corporate malfeasance. This is where the managers of corporate entities diverted from the interest of the owners of capital of profit maximization to serve their own selfish interests for personal gain (Donaldson and Davis, 1999; Bonazzi and Islam, 2007) and hence intervention and thereby founding of corporate governance. Under the agency theory, the management are usually agents (who posses particular technical skills and expertise on a relevant speciality) contracted

by the shareholders as principals (who are in possession of funds/ wealth in form of investments), to help them (shareholders) realize their ultimate goal of expanding their wealth/ investments with each party bound to meet its contractual obligations (Ping and Wing, 2011). Gomez and Russel (2005), trace the foundation of the agency theory to the 1932 works of Berle and Means which centred on the separation of the ownership and control of the corporate entities. Based on the agency theory is the agent-principal relationship where the principals' contract agents who are professionals to run their interests based on the expertise they possess (Abdullah and Valentine, 2009). And as a check to safeguard their interests the owners of wealth then choose amongst themselves members to sit in the board of their firm/s as non executive directors to monitor the performance of the agents/ managers (Donaldson and Davis, 1999).

According to Duke II, Kankpang and Okwonko (2012), there are times when complexities are encountered by shareholders in managing the agent- principal relationship with the agency costs then escalating as a result. Such agency problem/s then suffocates the performance of the firm as it gives the agents an opportunity to further wheedle out selfish personal gains from the firm (Tirole, 2005; Khan, 2011). This does not insinuate that the agents will not maximize the value of the owners' equity with such a set-up; in fact, they might be able to optimally perform their duties but also at the same time highly engage in pursuing their own selfish interests (Gul, Sajid, Razzaq, & Afzal, 2012). As such, Hart (1995) emphasizes that without the existence of agency problems corporate governance will not be necessary as the agents will carry out their duties as instructed hence no conflict of interests. Nevertheless, the author points out that agency problems do not solely justify the existence of corporate governance as there are also some other noteworthy factors in play.

2.1.2 Stewardship Theory

As per the stewardship theory of corporate governance, managers are not agents but competent stewards committed to maximizing the shareholders wealth (Letza and Sun, 2002). This view positions the stewardship theory as a challenger of the agency theory which portrays managers as untrustworthy and selfish (Gomez, 2005; Duke II and Kankpang, 2011). In this sense, managers are willing to voluntary act in the interest of their organizations and are not motivated by selfish interests as the agency theory portends (Benz and Frey, 2007). Abdulla and Valentine (2009), state that the stewardship theory is founded by psychology and sociology quoting the 1997 works of Davis and Schoorman who observed that managers as stewards get to make the most of their utility functions by maximizing shareholders wealth. While in accordance with the agency theory, agency problems emanate from the separation of ownership and control, the stewardship theory contests this view by stating that it was bound to happen since it facilitated proper management of intricate organizations (Learmount, 2002). The stewardship theory has had its share of criticism for example in assessing the position of the three key theories of corporate governance during the financial crisis that followed the bursting of the housing bubble of 2006, Wen and Zhao, (2008) observe a lack of stewardship indicated by the lack of accountability of directors and managers hence the need of having internal directors.

The proponents of the stewardship theory call for the presence of more insider directors in the boards of companies stating that such would lead to profit maximization as well as a more effective and efficient decision making mechanism (Letting et al., 2012). According to Donaldson and Davis (1991), the performance of a manager under the stewardship theory would then depend on the structures put in place at the location of the steward. The authors undertook a study on the effect of CEO duality on shareholder returns sampling 312 United States of

America corporations and found a positive between link between CEO duality and shareholder returns as advanced by the stewardship theory. In other words the research justified the stewardship theory which is in favour of the amalgamation of the role of the chief executive officer (CEO) and that of the chairman of the board of directors so as to bring down agency costs and at the same time enhance performance (Abdullah and Valentine, 2009). The principle behind the stewardship theory is centred on the premise that there is no need for external independent directors to bolster the monitoring and control of a firms executive as the management are trustworthy and capable of meeting their responsibilities (Heracleous, 2008) hence eventually bringing down agency costs (Wilcholson and Kiel, 2007).

2.1.3 Stakeholder Theory

The concept stakeholder theory was pioneered in 1984 by Edward Freeman who defined stakeholders as the individuals and groups who can influence or can be influenced by the undertaking/s of a corporation. In essence, the OECD principals of corporate governance 2004 classify stakeholders to include various resource providers such as investor's, employees, creditors and suppliers. The proponents of the stakeholder theory of corporate governance argue that while making key decisions, corporate executives should bear in mind the interests of all stakeholders (Boatright, 2006). This means that while the executives of the firm are striving to maximize shareholder wealth, they should also consider the interests of stakeholders, that is to say, balancing the interest of the two parallel parties (Lashgari 2004; Kahn, 2011). Even so, Heath and Norman (2004), point out that a number of the proponents of the stakeholder theory regard shareholders as just one of the major groups of stakeholders whose rights can be sacrificed in certain instances in order to discharge rudimentary commitments made to other stakeholders

Employees are among the most important stakeholders of corporate entities for the reason that they also bear the risks of insolvency with regards to the firm they labour for (Learmount, 2002). Therefore, as per the stakeholder's theory, proper management of the relationship between the firm and its stakeholders such as employees and customers will translate to the prosperity and success of the firm (Duke II, Kankpang and Okwonkwo 2012). But Health and Norman (2004) also caution that the stakeholder theory of corporate governance should not be applied overzealously as it might give managers the incentives to squander the firms' resources in the name of following the multiple objectives given to them under the notion of considering the interests of the various stakeholders. The Japanese, Continental Europe, and the German corporate governance practises are linked to the stakeholder theory in that their laws necessitate that a firm's workforce should be significantly represented in the board of directors, usually half of the seats of the boards (Nordberg, 2008).

Approaching this study from the stakeholder theory of corporate governance is fundamental especially since the demise of the Kenyan stockbrokerage industry between 2007 and 2010 mainly affected the Nairobi Securities Exchange investors who at that time were clients of the firms that went down. What is more, given the uncertainty surrounding the management of investors' funds in the Kenyan stockbrokerage industry, the stakeholder theory of corporate governance provides an impeccable basis of which corporate governance practices of these firms can be surveyed. For this reason, this study developed a framework that connects corporate governance practices of investor protection and the ownership structures within the Kenyan stockbrokerage industry. The forte of the stakeholder theory lies in the fact that it is regarded to intervene in solving the shortcomings of the other theories of corporate governance through the

directing company strategy to focus on all the groups of people who are directly or indirectly influenced by the undertakings of the firm (Ghayour and Doaei, 2012).[3]

2.2 Ownership Structure

Huafang and Jianguo (2007) studied the relationship between the ownership structure board composition and the degree of voluntary disclosure in 559 firms listed in the Shanghai Stock Exchange. The study which was carried out in 2002 arrived to the conclusion that high disclosure was linked with firms whose ownership structure was either higher block holder and/or foreign. On the other hand the same study found out that firms with managerial, state and or legal-person ownership were far from practicing voluntary disclosure. Mollah, Al Faroogue, and Karim (2012) comparably looked into the relationship between ownership structure, board characteristics, and financial performance for all firms listed in the Botswana Stock Exchange. The study which aimed to establish the function of corporate governance in the performance of listed companies found out that the concentration of ownership in firms such as institutional, government and foreign, is detrimental to the financial performance and the value of the firms. The study also revealed that dispersed ownership had the positive effect of enhancing the performance of the firm and at the same time mitigating agency conflict in the firms listed in the Botswana Stock Exchange.

Corporate governance practices relating to the ownership structure and their influence on the firms were observed to have a key impact on the economic performance of firms in Indonesia (Rusmin, Tower, Achmad, and Neilson, 2010). To be more specific, the study found noticeable disparities between the average returns on assets for non-family firms which were at 7.89%

[3] Corporate governance theories such as the agency theory has been understood to be only concerned with short-term goals of the firm disregarding the interests of other key players in the environment of the firm such as the employees, the customers/ clients and the general community in the firm's environ.

compared to family firms at 1.26%. The study went ahead to question the reason for this huge difference, probing whether it indicates a manipulation of figures by the controlling family entities? In Japan, a study assessing the effect of ownership concentration in dividend policy in Japanese firms found a similar scenario like in Indonesia where dividends proportionate to earnings were found to be lower in cases of ownership concentration (Harada and Nguyen, 2011). The findings further highlighted that firms with concentrated ownership were less likely to increase dividends when earnings increase or debts decrease.

Garcia-Meca and Sanchez Ballesta, (2011) undertake a study on the relationship between firm value and ownership structure of Spanish non-financial firms listed on the Madrid Stock Exchange during 1999-2002 and come up to a conclusion that ownership concentration influences the firm value. The study drew attention to the fact that controlling shareholders had the tendency of abusing their status at high levels of concentration rendering decisions that annihilate the market value of the firms. Likewise, Lemmon and Lins (2003) reiterate the iniquitous conduct of controlling shareholders during a crisis. Their study analysed the weight of ownership structure on the firm value during the East Asian Financial crisis that began in July 1997 using data from over 800 firms, all from the eight East Asian countries. The study revealed that the crisis raised the motivations for the minority shareholders to be expropriated by the controlling shareholders.

In the case of large shareholders, whether individual or institutional Gillan and Starks (2003) were of the view that they do have an important rule to play in the governance of firms. The authors conclude their study by stating that institutional shareholders/investors have the benefit of bringing about more informative prices, decreasing monitoring costs as a result promoting good governance. On the contrary, a study by Al-Fayoumi, Abuzayed and Alexander

(2010) that assessed the relationship between earnings management and ownership structure of Jordanian Industrial firms listed in the Amman Stock Exchange, between 2001 and 2005 find a positive link between insider ownership and earnings management. But also at the same time, the study found that both institutional and block holders do not commendably monitor due to lack of expertise or that they do engage in the malfeasance bandwagon same as the managers or they suffer from free rider complications.

In Korea, firms with concentrated ownership have been found to be in a have a tendency of benefiting from greater export performance than firms with diffuse ownership (Sangho and Donghyun, 2011). The authors were of the view that concentrated ownership has a positive effect as it encourages firms to engage in the export trade. And therefore accordingly, such firms played an important role in creating Koreas mark in international trade. In the issue of decision making and ownership structure, McCann and Vvoom (2010), evaluates management controlled firms against owner controlled firms arriving to the conclusion that management controlled respond more positively to the economic circumstances of the markets they operate in and therefore they have a tendency of being more profit making oriented.

2.3 Investor Protection

Rahim (2011) quotes the works of Carroll and Buchholtz (2008) who categorize ownership, interest together with legal and moral rights as the three sources of claims on the standpoint of a stakeholder in an organization. The author then draws attention to the role of the board in the organization of protecting interests of all stakeholders whose actions can affect the company or those who can be affected by the deeds of the company. Echoing the same observations, Klein, Mahoney, Mc Gahan and Pitelis (2012) identify that centering on the creation of stakeholders value as well rather than the traditional pursuit of shareholder value will

go along way in value creation of the firm. Such stakeholders oriented practice of corporate governance have been found to invest immensely in firm specific human capital than those firms that are shareholder oriented (Odaki and Kodama , 2010).

Successful firms like Google , Ebay and Johnson & Johnson among others have gone a notch higher to focus on more than their shareholders welfare and profitability of their firms, to incorporate the interests of their different stakeholders as part of their priorities (Freeman, Wicks and Parmar , 2004).In other words its better for a company to take into consideration the rights and interests of all value creating stakeholders rather than the shareholder approach adopted by a number of firms (Asher Mahoney and Mahoney 2004). Hemedoglu, Evliyaoğlu, and Arslantas (2012) examined the stakeholder relations of the companies in the ISE 150 index in the first quarter of 2011 and arrived to the conclusion that the companies had not matched up to the standards of investors relations required by the corporate governance principles prescribed by the Capital Market Board of Turkey. The CMB policy and procedures required that firms safeguard the rights of their employees and customers but it was realized that most of the companies have policies for their employees only but not for other stakeholders such as customer and suppliers.

In assessing the shareholder theory of the traditional Anglo American model of corporate governance practice and its shortcomings, Nwanji and Hotwell (2007), highlight the fact that since stakeholders play a part in the well being of the firm, the interests and rights of these stakeholders need to be seriously taken into account for the company to maximize the stakeholders wealth. The study also notes that the traditional Anglo-American model of corporate governance practices only focuses on the interests and rights of the stakeholder without any substantial address of the rights of the stakeholders. The advantages of this is that the cost of goods and services of such firms is much cheaper but the same firm stand to loose as stakeholder

focus has been found to increase the efficiency and market values of the firms that have adopted the practice (Allen, Carletti and Marquez, 2009).This shows that stakeholders model of corporate governance do play a major role in maximizing the wealth creation in behalf of the stakeholders (Yener, 2002).

Schilling (2000) draws attention to the works of Mary Follet (1918) who affirmed that the structure management and objectives of corporate entities can be reconfigured to fit into the needs and interests of the society surrounding it and this will in turn enable the business to meet its societal expectations. Interpreting Follets works, Schilling then describes that instead of working at manipulating managerial behavior or the influence of stakeholder groups focus should be directed towards improving the relationship between the managers of these firms and their different stakeholders. Pulling out from the perception of augmenting shareholder wealth to the goal of increasing and sustaining corporate value, Waldkirch (2008) asserts that corporate entities are mainly social ventures for mutual advantages to all persons.

A study of the relationship between stakeholders' interest and behaviour as well as performance of Norwegian banks between 1985 and 2002 found out that firms with diverse objectives out perform their counterparts having profit maximization as their only objectives (Bøhren and Josefsen, 2007). The findings of the authors insinuate that by firms adopting a corporate governance practices that attach importance to the rights and interests of several stakeholders then the particular stands to realize extra or additional profits. Nevertheless Boatright (2006) points out that such focus on stakeholder interests and rights by firms is the failure to recognize the different needs of the diverse stakeholder groups and as a result addressing the needs poorly. The author therefore stresses that the attempts that have been made

in addressing the interests of different stakeholders through the changes made in corporate governance policies have not been well formulated.

Donaldson and Preston (1995) on examining the three aspects forming the stakeholders theory, that is, its descriptive accuracy, instrumental power and normative validity resolve that a focus on the interest of stakeholders in the practice of corporate governance by firms doesn't fully guarantee firm performance and hence not a basis for stakeholder theory. However a study of the influence of the employees and shareholder interests in the dismal of 89 Chief Financial Officers (CFOS) of major Germany corporations between 1999 and 2006 found out that employee interests are given priority in the firm (Bremer, Ludtke, Richter and Schaffer, 2009). The study finds out that the stakeholders, specifically, both shareholders and employees wield significant power to control decisions on corporate governance practice. Stakeholder influence in firm performance was observed where it was found out that the CFOs and top executives have to take cognizance of the interests and rights of different stakeholders for them to safeguard their positions.

Jackson (2005) is of the opinion that a formidable employee "voice" together with investors engagement for greater corporate accountability will go along way in ensuring the future success of the company. Expanding the meaning of stakeholders to encompass other groups that can be affected by the activities of the corporations has overtime according to Barry (2002), brought about unworkable complications. The author goes ahead to give an example of shareholder activism which was once used as a tool of checking managerial conduct of the firm but has been abused of late to the detriment of the companies. This is contrary to the findings of Claessens and Ueda (2008) who studied the power of the role that multiple stakeholders play in firms and the channels through which such roles affect corporate performance. The authors

conclude their study by stating that the role of stakeholders in the performance of firms is poorly understood and that the area of study is in need of more research on a cross country basis evaluating the relationship between the different stakeholders as well as at firm level.

2.4 Conceptual Framework

The practice of corporate governance differs from region to region and from firm to firm. Nevertheless there are certain factors that have to be fulfilled in order to meet the standards of good corporate governance. These practices have to be characterized by the values of good corporate governance practices of fairness, transparency, accountability and responsibility. In other words, for any corporate governance practice to qualify as “good” the practices have to meet the threshold set out by the preceding four values. This study thus specifically examined two basic components on the practice of corporate governance in the stockbrokerage industry in Kenya. These two main components are ownership structure and stakeholder protection. The study surveyed how the Kenyan stockbrokerage firms practice corporate governance with these two main components of governance as the focal point.

2.4.1 Ownership Structure

Ownership structure takes quite different forms and by virtue of that diverse firm attributes. This is because shareholders of a firm do elect/nominate directors who then appoint managers to run the corporations under the supervision of the board. Firms are ordinarily owned by insiders/ managers, the government, institutions/ organizations, non-nationals (foreign person/s or institutions) and diverse/diffuse ownership. Under the ownership structure is also the concentration which is essentially defined by the percentage of shares owned by the shareholders. Managerial ownership is where the managers of a firm are given a stake in the

business they manage. This move has been said to increase the value of the firm but too much of insider ownership might also increase the tendency of managerial entrenchments (McConnell, Servaes and Lins, 2008). Government owned institutions also known as parastatals are either fully owned by the government or the government is the majority shareholder. These parastatals have over time been mostly associated with overdependence on huge government bailouts and subsidies, political psychofancy and colossal malfeasance (Gakeri, 2011; Adeyemo and Salami, 2008; Cao, 2001).

Institutional ownership comes about when established institutions either set up companies or buy stake in companies hence being part of the shareholding. This type of shareholding has the detrimental potential of transferring the risk taking orientations of the shareholding company to the affiliate firm (Ongore, 2011). This would then mean that if the shareholding firm is risk taker this trait will be customarily transferred to the affiliate firm and vice versa. Other potential implications of such institutional ownership include the possibility of the shareholding firm using the affiliate firm for money laundering and tax evasion.

Foreign investors whether individual or institutional have been proven to improve on the practice of corporate governance in firms. For example such foreign investors usually call for greater legal protection of their interests and sound corporate governance mechanisms in order for local business climate to attract them (Gillan and Starks, 2003). Foreign ownership has also been associated with some degree of performance enhancement of firms notably refining on the supervision and performance based motivation of the managers in addition to the introduction of modern technology and globally tested management practices to the firm (Ongore, 2011; Bebchuk and Roe, 1999).

Diverse/diffuse ownership is whereby a firm/s is owned by small shareholders who are geographically scattered. Gillan and Starks (2003) are of the view that such a setup is deficient of motivating the shareholders to actively monitor the firm's management as the individual shareholders will solely shoulder the monitoring costs and in spite of that, gains from such enthusiastic monitoring will accrue to all the shareholders. This therefore has resulted to poor performance of firms with such shareholding structures (Ongore, 2011). This emanates from the fact that the lack of proper monitoring leaves the managers with a lot of discretion in the performance of their duties. It is therefore easier for managers in such a setup to divert from pursuing the interests and wishes of the owners of wealth to chasing after their own selfish rent – seeking endeavours.

A firm's ownership is concentrated if the first five major shareholders hold a total of more than 30 per cent of the entire issued shares. Ownership concentration affects key decisions of a firm in a number of ways. For example, studies have shown that leverage decreases with ownership concentration and furthermore in case of takeovers or acquisition of the firm, few majority shareholders may find it easy to direct such activities towards their desired goals , that is, either resist to preserve jobs or approve such acquisition in case the block-holder stands to benefit (Holderness, 2003).This brings out the fact that with concentrated ownership, the block holder wields a great deal of influence in monitoring the management, gaining access to valuable information, and making key governance decisions (Desender, Garcia-Cestona, Crespi and Aguilera, 2009). With such influence, Ongore (2011) points out that this might be employed by the block-holders to effectively monitor the management company leading to exceptional performance but also such influence might be abused to the extent that it limits managerial

discretion making the decisions of the top executives and the firm at large to reflect the risk taking comportments of the block-holders.

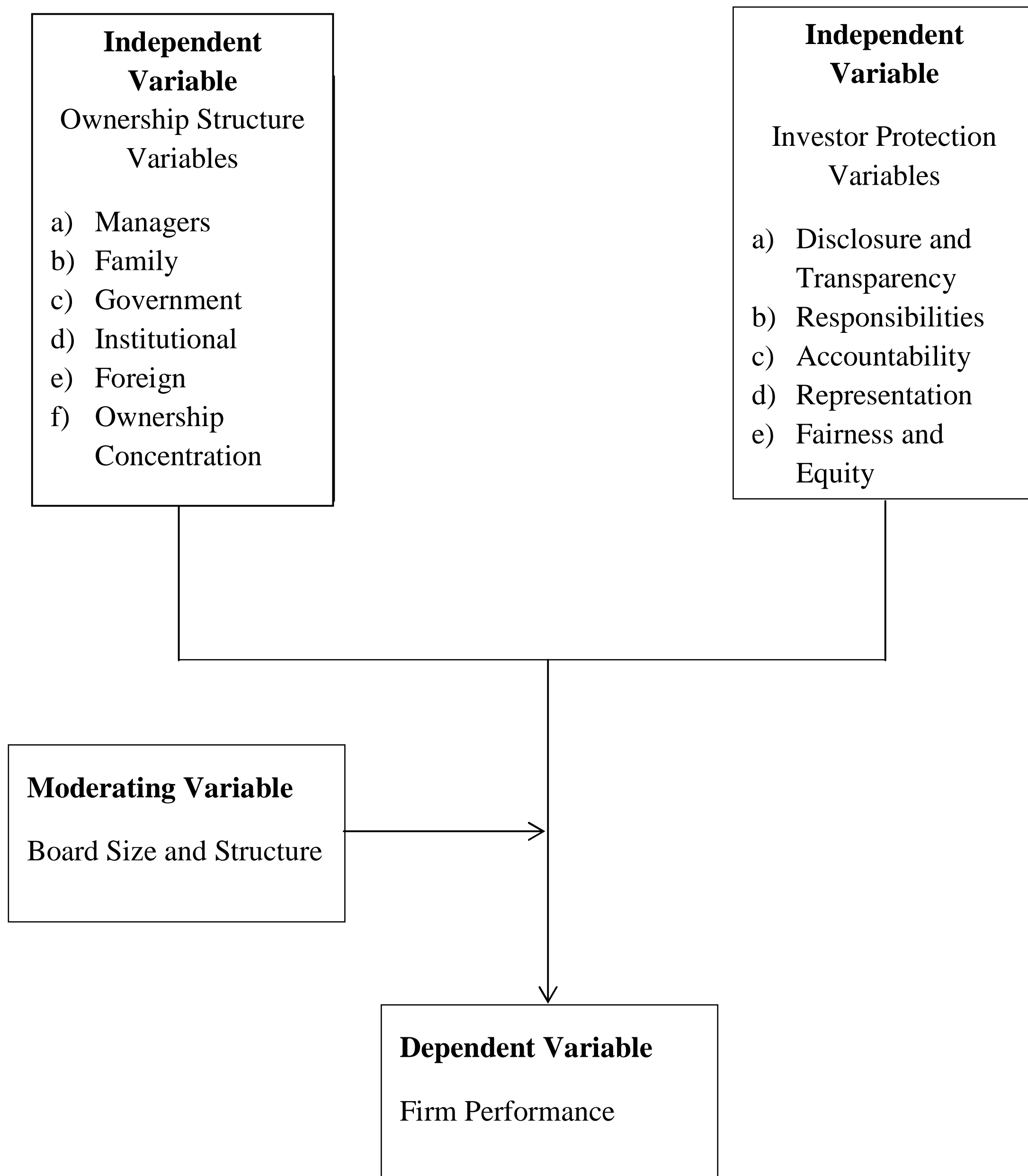
2.4.2 Investor Protection

The stakeholders of a firm are persons who can be affected by the activities of the firm or whose activities affect the firm's performance. Stakeholders interests in the firm should therefore be taken into consideration in the practice of corporate governance and these stakeholders include investors, managers, employees, customers, suppliers, business partners and local communities (Nam and Katu, 2004). This study mainly focuses on the protection of customers of the stockbrokerage firms who do invest in the Nairobi Securities Exchange through the firms .The study examines the corporate governance practices of firms from the mainstream stockbrokerage industry in Kenyans with regards to their efforts in the protection of the interests of their clients. This emanates from the fact that clients as stakeholders do contribute to value creation of the firm and if the firm's stockbrokerage were to collapse then there is a chance the investors would lose their investment or if not the value of their investments.

Research has indicated that stakeholder oriented firms will prosper if competing against the shareholders oriented firms (Ginglinger, Megginson, and Waxin, 2011). This will be the case especially in a competitive environment where the direct stakeholders such as clients /customers have alternative or substitute firms to choose from (Andersen, Holmström, Honkapohja, Korkman, Söderström, and Vartiainen, 2007). Some have argued that shareholders interests and rights should be given priority over the rights and interest of the rest as the relationships and interests of the rest of the stakeholders such as suppliers, employees and customers are well laid out, protected and defined by contracts entered between the firm and themselves (Baums and Scott, 2003).

All in all, shareholders have invested in the firm which without the clients the firm would not realize any economic value. This is to say that in the stockbrokerage industry the clients have as well invested same as (and it might turn out be more than) the shareholders of these intermediaries. The shareholders have appointed the board to monitor the conduct of management in the business and ensure that their interests are protected. What about the clients of these firms who have a lot to loose in case of mismanagement? Selected authors have advanced their arguments that a firm is the product of a principle plus an environment (Koyama, 2010). This means that shareholders invest in the firms the principle but the environment (meaning the community around the employees, the customers etc.) invests on intangible assets. From this perspective, the shareholders and stakeholders interests are the same for both of them long for the firm to thrive in the competitive business environment for their individual gain (Carrillo, 2007). In the case of the stockbrokerage industry, the customers also invest their money in the firm in order for the firm to generate profit as well as earn the customers an income from their investments. And this is why Bajpai (2005) was of the opinion that in corporate governance practice the interests and rights of contractual stakeholders such as customers, employees and vendors should get precedence over the rights of the owners of equity.

FIGURE 1
Conceptual Framework



From the above model:

A. Independent Variables

i) Ownership Structure Variables

Indicators:

a) Managers
b) Family
c) Government
d) Institutional
e) Foreign
f) Ownership Concentration

ii) Investor Protection Variables

Indicators:

a) Disclosure and Transparency
b) Responsibilities
c) Accountability
d) Representation
e) Fairness and Equality

B. Moderating Variables

i) Board Size and Structure

C. Dependent Variables

i) Firm Performance

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Research Design

An excellent research study makes use of a research design that is most applicable to its object rather than the "perfect fit" (Tashakkori and Teddlie, 2009). This means that the researcher needs to be thoroughly exposed to a vast range of research methodologies for him/her to select the most appropriate design or combination of designs (Groenewald, 2004; Hoddinott and Pill, 1997). In this respect, the study is both qualitative and quantitative in design, to be precise, mixed research and was carried out by exploring, investigating and in the end, described the practice of corporate governance in Kenya's stockbrokerage industry. Thus the research as a survey collected data from the firm members of the Kenyan stockbrokerage industry. In doing so, the study provides an in-depth comprehension of the present-day practices of corporate governance by the Kenyan stockbrokerage firms focussing on the ownership structure and the initiatives employed by the firms in seeking to safeguard the interests of their clients (Investors).

3.2 Population

The study population comprised of 10 firms out of the 11 companies forming the mainstream stockbrokerage industry in Kenyan based on the list made available by the Capital Markets Authority as at July 30th 2012. The study is based on information from senior and/or middle level executives of the stockbrokerage firms with a profound comprehension on the operations of the industry and their firms in general. Because of their expertise, this class of population is expected to provide niche information based on their proficiency in the industry. In

only in one case that the response from the first respondent was not adequate enough, hence the researcher gave an additional questionnaire to separate executive in the firm. This was in a bid to access actual data from the respondents on the practice of corporate governance at firm level.

3.3 Pre-Testing, Reliability and Validity

Due to the complexity surrounding corporate governance issues and the difficulties associated with accessing some of the subjects (who in this case were executives in the firms) with sufficient comprehension of the doctrines of corporate governance practices, it was deemed crucial to carry out a validity test as well as a reliability test. The final questionnaire was constructed, reviewed by an expert in the area of corporate governance, and then administered to three respondents each selected on stratified basis from different stockbrokerage firms. Of the three respondents, one was a finance executive, the other was a legal/ compliance executive and the third respondent was a chief executive officer of the stockbrokerage firms. The respondents were then asked to respond to the questions depending on their comprehension and where possible, suggest on how the questionnaire can be improved. The responses to each of the questions in the questionnaires was then scrutinized and modified until the researcher became satisfied that it is an accurate measure of the desired construct, and that there is adequate coverage of each area to be investigated. The process was then repeated again with a new set of respondents from stockbrokerage firms different from the initial test. On evaluating the responses the researcher considered whether the respondents understood the questions in the questionnaire and that they possessed the knowledge or memory to respond to the questions accurately. Additionally, given that corporate governance is a very sensitive issue especially in a recovering sector such as the Kenyan stockbrokerage industry, the "fear of reprisal" by the respondents was noted to be prevalent and this had the potential

of influencing the validity of the survey results. Therefore in order to resolve this, the researcher guaranteed the respondents a high level of anonymity and lower chances of reprisal.

In a pragmatic research, subjects are usually chosen according to their usefulness in aiding the researcher achieve the research objectives (Mack, Woodsong, MacQueen, Guest and Namey, 2005; Owen and Chandler, 2002), and by this the researcher conducted a reliability test alongside the validity test. The reliability test was conducted using the test-retest method where a pilot test collected data from 3 subjects, who did not take part in the final survey. Data collected from pilot test was recorded and then after 2 days the same subjects were asked to complete the questionnaires. The responses from both the pilot test and the subsequent test were then evaluated by the researcher. From the examining the data, a consistency of 95% was noted and therefore the instrument for carrying out the survey was deemed satisfactory for its intended purpose. The biased selective of subjects to respond to the questionnaires played a significant part in the productivity of the findings of this study by virtue of the quality of information gathered from the well-informed experts (Tongco, 2007).

3.4 Data Collection and Management

This study used both primary and secondary data. Data collection was specifically handled by the researcher to save on costs and time of acquiring data as well as ensuring that data relevant to the study is gathered. Primary data was collected through structured self-administered questionnaires on the executives of the mainstream stockbrokerage firms in Kenya. The questionnaires were administered directly to the subjects with brief instructions on how to respond to the questions. Once the 11 (eleven) licensed stockbrokerage firms to be studied were established, the study selected at-least one executive per firm to be supplied with the questionnaire. In total, 12 questionnaires were received from 10 (ten) firms out of the eleven that

constitute the industry, meaning that two firms out of the ten responded to two questionnaires. Each of the employees from the 10 (ten) firms were supplied with the questionnaires together with an explanation on what each of the question in the questionnaire requires. Interviews which were to be employed in cases where the respondents did not properly comprehend the questions were not used since the respondents were instructed on what each and every questions in the questionnaire requires. Secondary data from published academic journals and periodicals, legal encyclopaedia, and institutional publications (Greener, 2008) was evaluated alongside the data from the primary collection of data (Savenye and Robinson, 1996). These secondary data sources helped to clarify and critically evaluate subjects that might not have been fully addressed by primary data. This cadre of data was mainly accessed through online information data banks.

3.5 Data Analysis

According to Bong (2002), the method of data analysis employed in a research should be selected as a result of the form of research design undertaken. This study used both closed-ended questions and open-ended questions. Closed-ended questions were used to develop preliminary themes using descriptive statistics as a form of quantitative analysis. The open-ended questions which allowed the respondents to provide in-depth responses provided qualitative data which was analysed using content analysis. Mayring (2000) and Elos and Kyngas (2008), identify two approaches in the use of content analysis, that is, inductive content analysis and deductive content analysis. In this case, the study made use of the inductive content analysis for the qualitative data and univariate analysis as a form of descriptive statistics for the quantitative data.

In the case of qualitative data, the researcher was able to finally developed themes from information emerging out of the analysis. The themes are what were used to then develop the underlying assumptions regarding the corporate governance practices in the stockbrokerage

industry in Kenya. The inductive content analysis approach used in this study was designed by Thomas (2006) who identified three steps involving; (i) condensing of raw textual data into a brief, summarised format; (ii) setting up of clear links between the research objectives and the summary findings derived from the raw data; and then (iii) developing a framework of the fundamental structure of experiences evident in the raw data.

Upon the collection of the completed questionnaires, raw data from the responses to the questions contained in the collected questionnaires was systematically examined. After going through the questionnaires, similar responses were condensed and then grouped into different inputs. Each input was allocated a unique identification code and the codes were grouped next to the appropriate segment of the inputs. After the researcher was satisfied that all the collected raw data had been exhaustively summarised as inputs and then coded, inputs relating to each other were then grouped together and then the codes were arranged alphabetically. Once the categorization of the responses from the questionnaires was saturated, the inputs were then narrowed down into 26 sub-themes. The different Sub-themes were then classified into main themes which were then broken down in order to reveal the underlying assumptions. The theories from the analysis were in the end integrated as findings of the study. This choice was based on the fact that the inductive content analysis allowed the researcher to develop a concrete concept out of the data collected (Elo and Kyngas, 2008).

CHAPTER FOUR

FINDINGS AND DISCUSSION

4.1 Introduction

This study surveyed corporate governance practices relating to the ownership structure and investor protection in the Kenyan stockbrokerage industry. Ten out of the eleven firms comprising the Kenyan stockbrokerage industry were surveyed. The respondents in charge of compliance in the stockbrokerage firms provided first-hand data to the questions inquired in the questionnaire administered by the researcher. As indicated earlier the need for conducting further interviews for the purpose of acquiring additional data did not arise as the data provided in the questionnaire was deemed sufficient for the survey. The collection of data took an average of 4 days where all the respondents had completed filling the questionnaire. This was achievable since each of the respondents was given a brief explanation on what each question required in a bid to ensure that the respondents comprehend what is expected of them along with making certain that all the information collected was relevant to the objectives of the study.

The research questionnaires used mixed questions containing both closed and open ended questions. The questions required " yes" or " no" response from the respondents and some giving the respondents an opportunity to come up with his/her own response increasing the accuracy of the results as well as the success of the study. A total of ten out of the eleven member firms of the stockbrokerage industry agreed to take part in the survey by responding to the questions in the questionnaire regarding their practice of corporate governance in their structures. The collection and analysis of data was conducted solely by the researcher with the respondents from the ten stockbrokerage firms' completing the questionnaire from their registered offices in Nairobi. The questionnaires were mostly completed by finance executives (6 out of 10 firms) and

also executive officers in charge of compliance (3 out of 10 the firms) the Chief Executive Officer (1 out of 10 firms). The firm that declined to take part the survey indicated confidentially and the sensitivity of issues of co-operate governance in the stockbrokerage industry as the main reason for their refusal.

TABLE 1
Percentage of Respondents Who Completed the Questionnaire(S)

Respondents	Number of Firms	Percentage
Finance Executives	6	60
Corporate Compliance Executives	3	30
Chief Executive Officers	1	10
Total	10	100%

Out of the ten firms surveyed six had an in – house corporate governance policy while the remaining four out of the ten firms did not have. Unexpectedly, none of the ten firms surveyed had ever been fined for non-compliance of corporate governance policies. In this question, the firms were required to state whether they have ever been fined by the market regulator, that is, the Capital Markets Authority for non-adherence to the corporate governance regulations and all the firms responded "NO". Six firms out of the ten stated that their net profit in the most recent declared annual financial results was less that 20 million shillings while three out of the remaining four declared that their profits in the same period was between 21 to 40 million and only 1 firm out of the ten surveyed had net profits of more than 100 million Kenya shillings. Out of the 10 respondents 5 were female and 5 were male and all the respondents had attained graduate degree and above. The study was conducted in two main phases the administering of the questionnaires to the respondents and the analysis of secondary data.

TABLE 2
The Firms Net Profit in the Most Recent Declared Annual Financial Results

Net Profit (in Million Kshs.)	Number of Firms	Percentage
Under 20	6	60
21 - 40	3	30
Above 100	1	10
Total	10	100%

1. Investor Protection

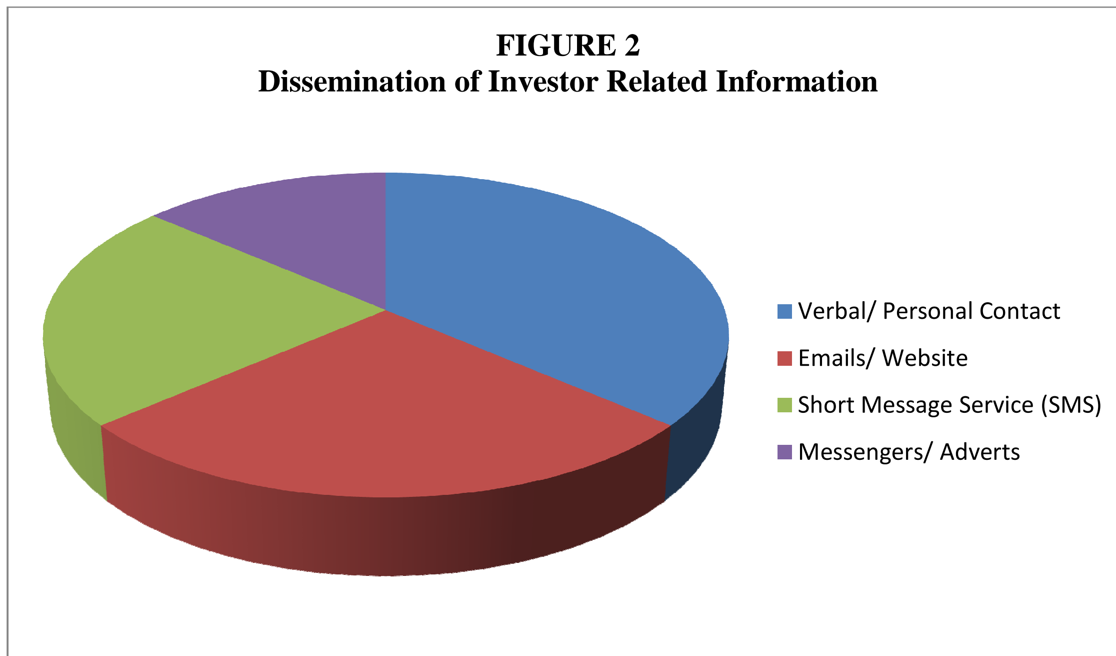
Of the ten stockbrokerage firms surveyed only one had clients numbering between 1,501 and 2000, while each of the remaining nine firms had more than 2000 clients in number. The same stockbrokerage firm with the least number of investors in the group obtained net profits exceeding 100 million shillings in the most recent declared annual financial results with the next closest firm having net profits between 21 to 40 million shillings while the rest having net profit less than 20 million Kenya shillings. All the firms responded in the affirmative to the question on whether they prioritize the interests of their clients/ investors in the practice of corporate governance. Similar response were also noted when the respondents were asked whether they have policies that seek to protect the interests of their clients investors as key stakeholders of their firms.

When asked about the basic rights that their firm's clients are provided with, diverse observations were made. Of the ten firms only five responded to practice fairness and equity among the rights afforded to their clients. The practice of these firms focused on the equal treatment of all shareholders in accessing their services. Six firms out of the ten firms surveyed highlight disclosure and transparency in providing services to their clients. This was particularly noted in access of information where the six firms stated that their clients had the right to access different types of information with regards to their investments. Only three out of the 10 firms

surveyed recognized fulfilling their responsibilities to their clients in an efficient and effective way as an obligation.

TABLE 3
Dissemination of investor related information

Forms of Dissemination	Number of Firms
Verbal/ Personal Contact	8
Emails/ Website	6
Short Message Service (SMS)	5
Messengers/ Adverts	3



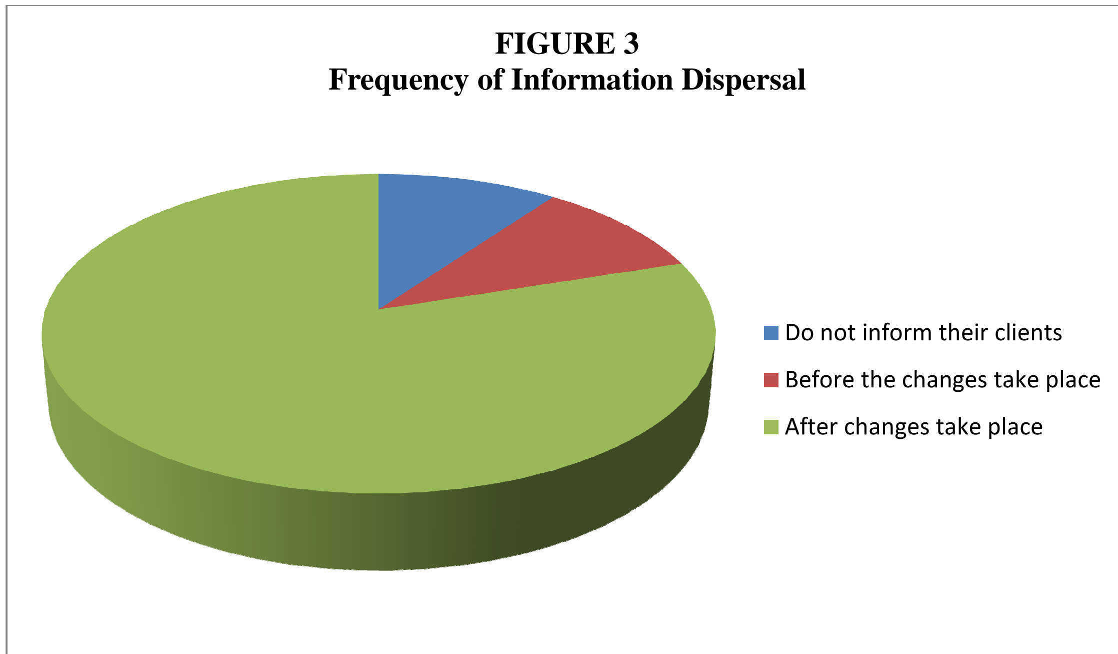
All the firms do not have representatives of their clients on the board and on the question on how the interests of the clients are represented in the company only three out of the ten questionnaires were answered. Respondents from these two companies responded that they created the customer relations department to be responsible for the interests of the clients while the respondent from the third firm responded that compliance of rules and regulations ensures

that their clients' interests in the company are well taken care of. In response to the question on how the firms impart information to their clients regarding their privileges and roles in their governance, verbal/ personal contact was the mostly used with eight out of ten firms making use of it. Emails or the use of the firm's website came second with six out of the ten firms using it. Five out of the ten firms used the short messaging service (SMS) via mobile phones while three out of the ten firms use messengers or adverts to impart such information.

On the question concerning the measures put across to ensure efficient and timely access to information it was noted that the respondents ended up giving answers that they had given in a previous question. Only one out of the ten firms responded that they do not inform their clients of any corporate changes in the question enquiring if the firms informed their clients of any corporate changes and how the clients are informed. Of the 9 firms that responded in the affirmative, only one firm informed its clients before any changes took place while the rest of the firms informed their clients after the corporate changes took place with a respondent citing that the information is passed over to the clients after the approval of the Capital Markets Authority which is the regulator of the Kenyan securities markets. Emails were the mostly used means of relaying such information with six firms using it while the least used model of relaying information was the post and messengers or agents with 2 firms using each of the modes. Four firms responded that they do use the media to inform their clients of any corporate changes.

TABLE 4
Frequency of Information Dispersal

Mode of Dispersal	Number of Firms
Do not inform their clients	1
Before the changes take place	1
After changes take place	8



Finally when asked which particular corporate governance practices the respondents thought was superior, only two out of ten firms responded that focusing on the interests of external stakeholders ,that is, the neighboring community and clients etc. was best. The rest of the respondents from the eight remaining firms were of the opinion that balancing between the interests of both the both the internal and external stakeholders was the best corporate governance practice. Two firms out of the ten surveyed responded that they had corporate governance practices that reflected the local regulatory frameworks and the international principles. On the question regarding the information update to their clients, four out of ten firms updated their clients on monthly basis while three of the stockbrokerage firms updated their clients on weekly or daily basis. The other forms of updates were only employed or adopted by three firms out of the ten.

TABLE 5
Frequency of Information Update

Interval of Dissemination	Number of Firms
Monthly	4
Weekly/ Daily	3
Others	3

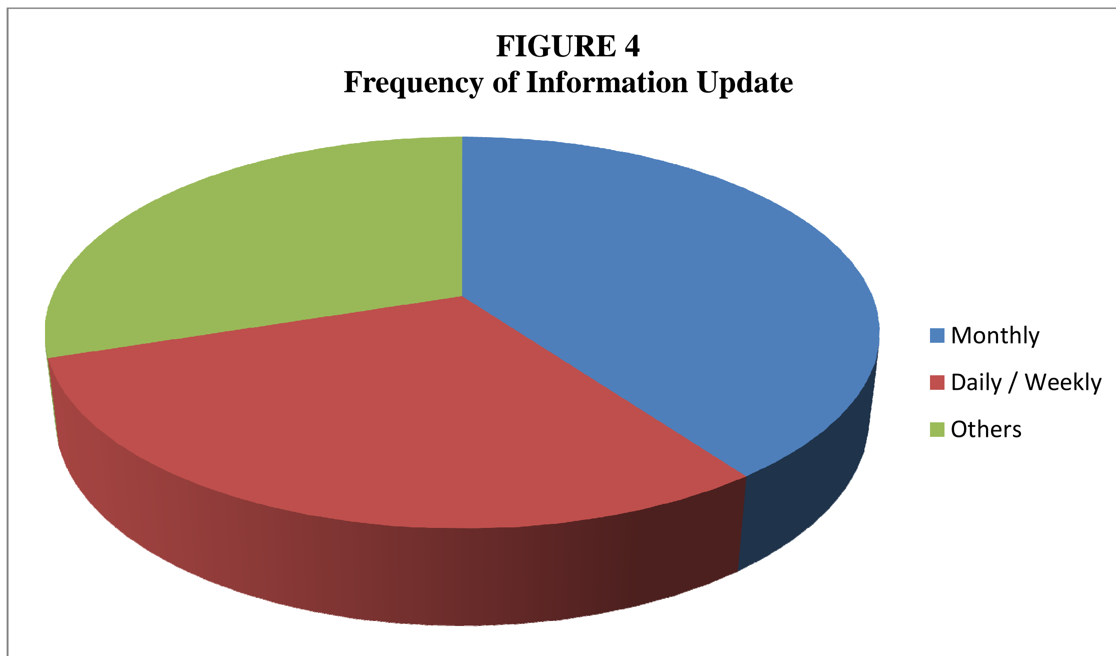


FIGURE 4
Frequency of Information Update

2. Ownership Structure

On the ownership structure of the ten firms surveyed, the respondents were to assess the ownership structure of their firms based on either family, insider, dispersed, diverse, institutional, foreign or other forms of ownership summing up to 100 percent of the total issued shares. Only one out of the ten firms had insider (managerial) ownership where an executive in the firm owned 10 percent of the total issued shares. Family ownership in the firm's survey was prominent with seven out of the ten firms at least having family shareholding structure. Two out

of the seven firms were fully (100 percent) owned by families. Of the remaining 5 firms one had a family shareholding of 50 percent followed by one with 30 percent and then one with 25 percent, one with 10 percent and the least percentage of family ownership of the total firms surveyed being 5 percent. It's important to note that such firms with family ownership have employed one or two of their family members in executive positions in the firms probably to safeguard their interests in the firms.

TABLE 6
Forms of Ownership Structure in the Industry

Forms of Ownership	Number of Appearance on Firms
Managerial	1
Family	7
Institutional	4
Diverse/ Diffuse	5
Other Forms	2

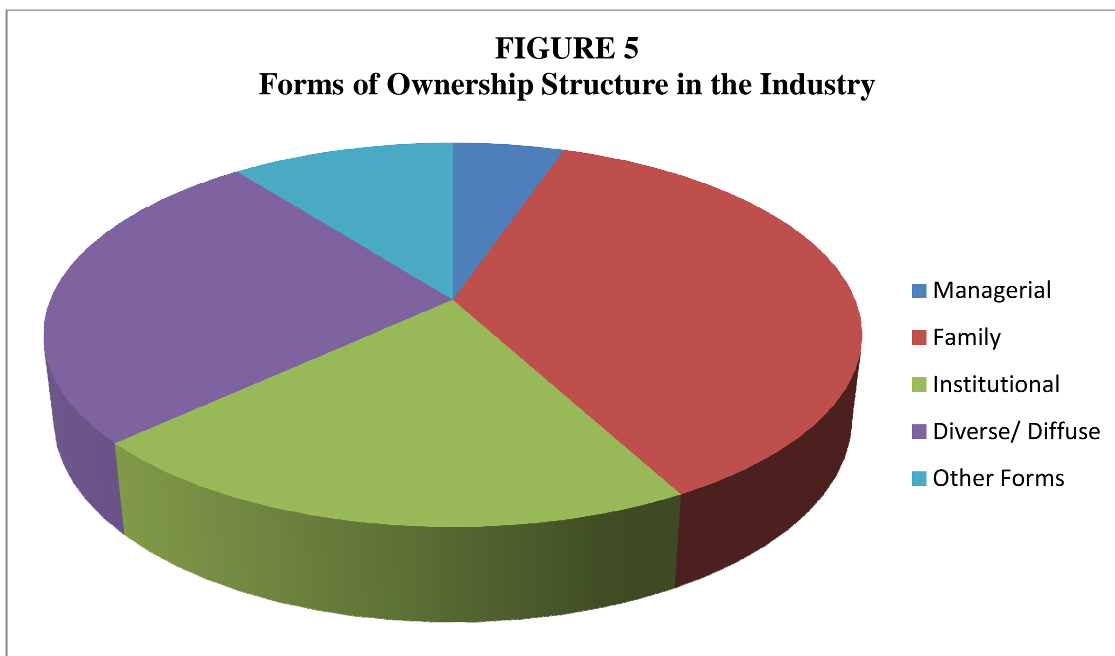


TABLE 7
Managerial Ownership

Number of Firms	Percentage
1	10

Of the ten stockbrokerages firms surveyed, four had institutional shareholders. And out of these four stockbrokerage firms, one had shareholding of 100 percent while the second firm in this category having a 91.3 percent institutional shareholding. The rest of the two firms having institutional shareholders had a 70 percent shareholding each. In the case of diverse/diffuse ownership, five stockbrokerage firms out of the ten had such a structure with the highest shareholding being 100 percent, followed by 95 percent shareholding. The rest of the firms had a diffuse shareholding of 50 percent, 40 percent and then 10 percent. Diverse/diffuse ownership is where a company is owned by small shareholders who are scattered geographically. Lastly two stockbrokerage had other forms of shareholding which was at 8.7 percent and 10 percent.

TABLE 8
Family Ownership

Number of Firms	Percentage
2	100
1	50
1	30
1	25
1	10
1	5

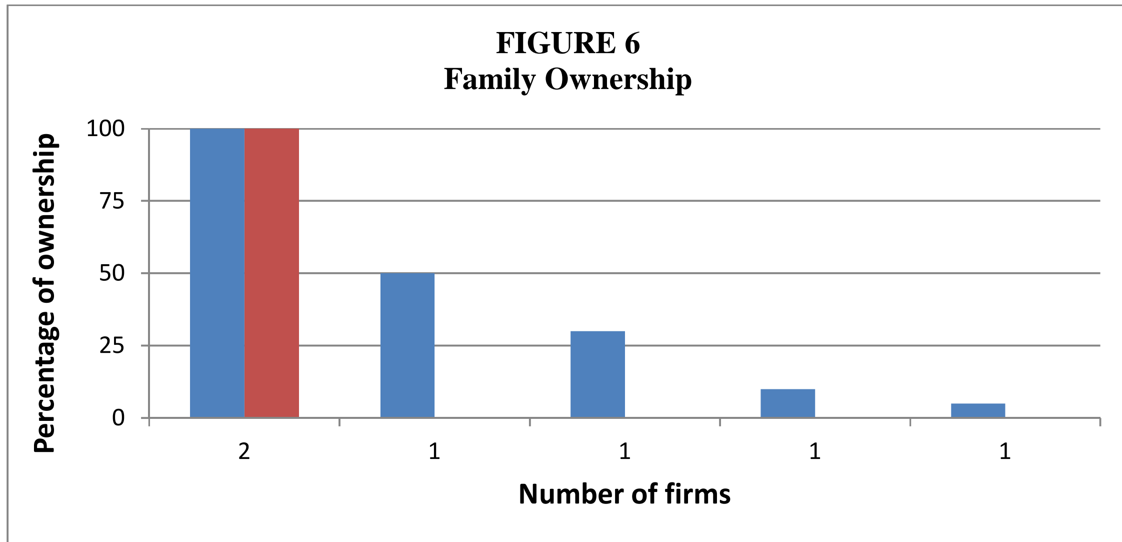
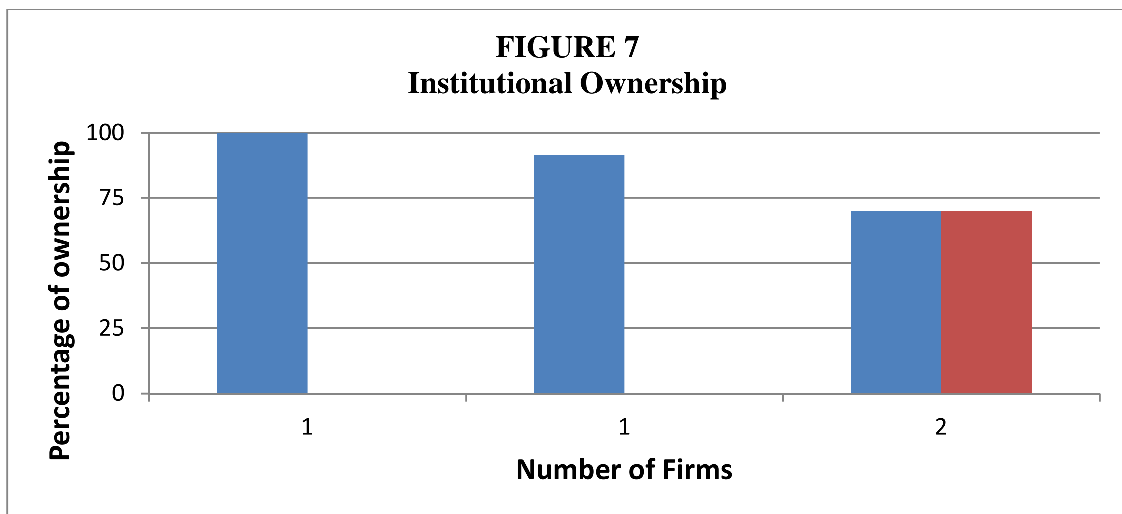


TABLE 9
Institutional Ownership

Number of Firms	Percentage
1	100
1	91.3
2	70



On the question on the series of shares in terms of voting rights all firms responded affirmatively that they do have only one series of shares. This question required the respondents to choose whether their firms had; only one series of shares; two series of shares each with different voting rights; or three or more series of shares each with different voting rights. Five out of the ten firms responded to the question on whether there are any affiliations among the shareholders of the companies. Out of the five, two firms responded affirmatively that there are affiliations among their shareholders while the remaining three firms responded that they do not have any affiliations among the shareholders. Eight firms out of the ten surveyed responded to the question on the existence of nominee holdings in the ownership structure of the firms. Out of the eight firms only one firm responded affirmatively on the existence of nominee holdings in its ownership structure while the rest of the respondents stated that their ownership structure does not have nominee holding. Finally on whether there are any director shareholdings in the ownership structures of their firms, eight firms responded out of which, 7 responded affirmatively while only one firm out of the eight that responded did not have director as shareholders.

TABLE 10
Diverse/ Diffuse Ownership

Number of Firms	**Percentage**
1	100
1	95
1	50
1	40
1	10

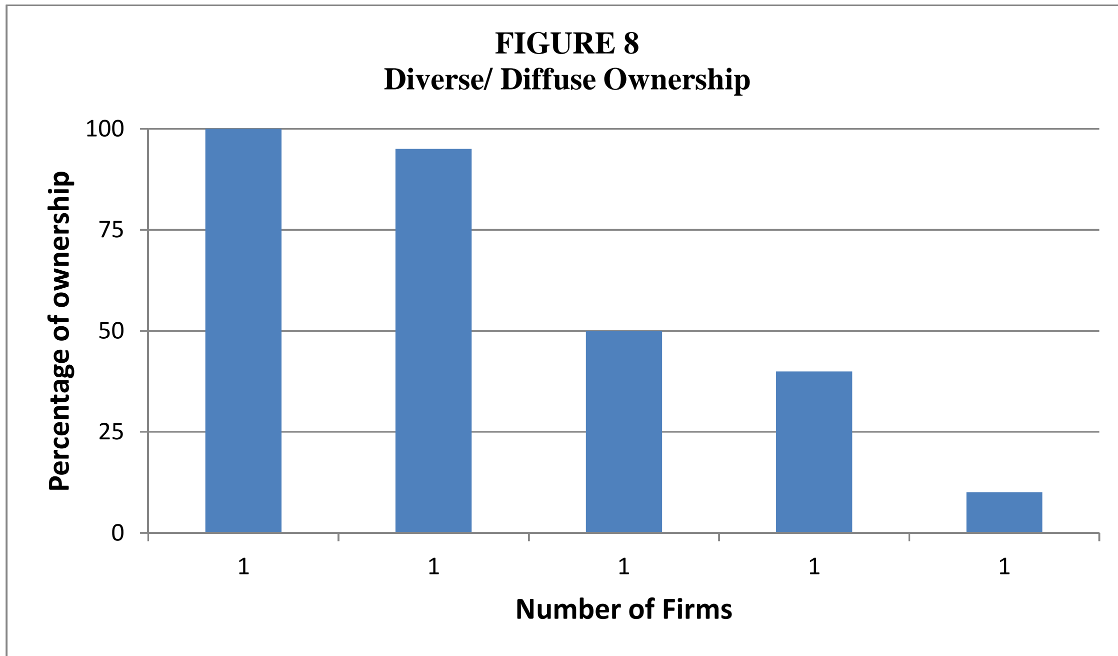


TABLE 11
Nominee Shareholding(s)

	Number of Firms
Yes	1
No	7
Did not Respond	2

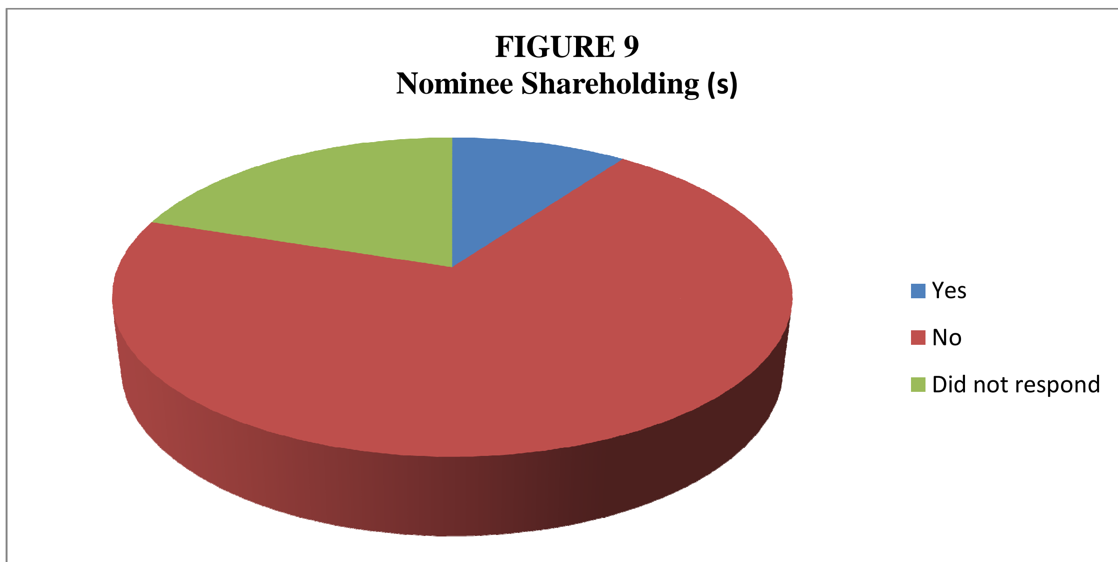
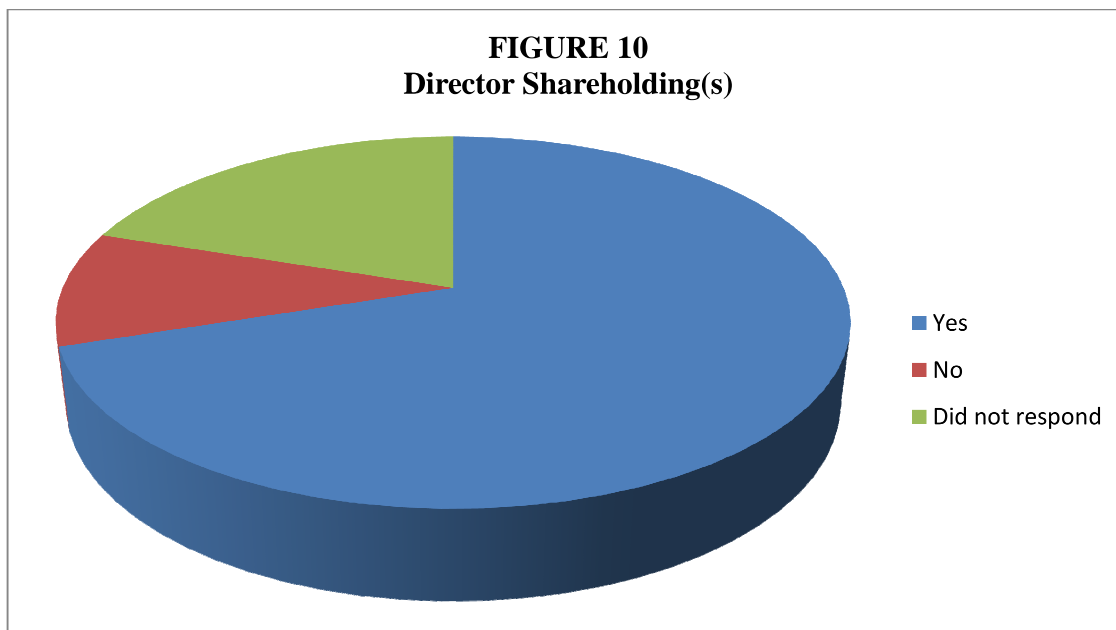


TABLE 12
Director Shareholding

	Number of Firms
Yes	7
No	1
Did not Respond	2

FIGURE 10
Director Shareholding(s)



4.4 Finding Related To Research Questions

4.4.1 What is the Current Ownership Structure of the Firms in the Kenya Stockbrokerage Industry?

The ownership structure of ten firms surveyed through questionnaires mainly based on family ownership, insider ownership, diverse/diffuse ownership, institutional ownership, foreign or other forms of ownership structures as indicators. The findings of the study indicate that the Kenyan stock brokerage industry is highly concentrated with the family as well as institutional ownership structures dominating the industry. Out of the ten firms surveyed seven had the

presence a family shareholding with two firms being owned 100 percent by a family. The least percentage of family shareholding in this case was 5 percent. Under the family ownership structure two other firms also have shareholdings that are above 30 percent , that is, 30 and 50 percent respectively. Normally a firm is said to be concentrated when the first five major shareholder hold 30 percent or more of the issued shares. The Herfindahl index (Herfindahl–Hirschman Index or HHI) is used to measure the concentration of ownership in a company.

On the same note, institutional ownership dominates the industry with four firms out of the ten surveyed having institutional shareholders. In this case the institutional shareholders are either commercial banks or investment banks operating in Kenya. One of the firms was found to be 100 percent owned by an institution which is closely followed by a 91.3 percent ownership of another stockbrokerage firm and then the other two firms being owned 70 percent each by institutions. The case of the dominance of both institutional and family shareholding in the Kenyan stockbrokerage industry leaves insider ownership with only with 10 percent held in one firm. Four firms out of the category of dispersed /diffuse ownership have shareholdings above 30 percent to be precise, 40 percent followed by 50 percent then 95 percent and then the highest being 100 percent. The existence of nominee holdings in one of the stockbrokerage firms makes it difficult to structure the ownership concentration of such a firm. The results of the survey therefore indicate that there is a high concentration of ownership in the Kenyan stockbrokerage industry, with the most dominant ownership structures being the family ownership together with institutional ownership.

4.4.2 What Are The Prevalent Investor Protection Practices Of The Stockbrokerage Firms In Kenya?

Most of the ten stock brokerage firms in Kenya have clients numbering to more than 2000. In fact only one of the firms has clients between 1,501 and 2000. Nevertheless, from the data collected, a huge difference is noted in terms of net profit with the firm having the least number clients realizing net profits over 100 million Kenya Shillings (Kshs) and the next firm with profits close to it having between 21 and 40 million Kshs after that the rest of the firms having profits under 20 million Kshs. Majority of the firms in the stockbrokerage industry recognize the importance of considering stakeholders interests in the practice of corporate governance as one firm responded that focusing on the interests of external stakeholders (the community around the company and the clients) was requisite for good corporate governance practice while the rest responded that a balance of the interests of both the external and internal stakeholders was key to good corporate governance practice.

From the results, all the stockbrokerage firms comprehend the relevance of investors/clients in the well-being of the firm in such a competitive industry, which is for business reasons. This was noted after the firms responded that they do “frequently” update their clients on information regarding their investments. The frequency ranges from firm to firm with the least frequency per year being monthly while the most active clients’ accounts being updated daily and weekly. According to the data collected, the Kenyan stockbrokerage industry prefers to update their clients in person as eight of the ten companies use personal updates as the primary mode of communication. On the upside, the industry has embraced modern technology in communicating with their clients as six of the ten firms used emails to communicate with the clients with the remaining four using text messages. Three of the firms still use the traditional

methods of agents and adverts in communicating with their clients. On the mainstream corporate governance practices, the results indicate that only two firms out of ten responded that they to follow the local regulatory framework while the rest of the firms responded that their practice/s reflected both local and international practices. However, when asked which international guidelines they do adhere to only one firm was able to respond to that. Based on the findings all the companies are not aware of the globally accepted guidelines of co-operate governance such as the Organization of Economic Cooperation and Development (OECD) principles of corporate governance, 2004. On their daily operations these firms complied with the local regulators framework and hence practiced corporate governance. This therefore meant that the industry was conscious of the statutory requirements to practice good corporate governance especially in their industry but had not yet full comprehended the fact.

The lack of adequate response from the firms' on the question regarding measures that have been put across to ensure the efficient and timely access of information by their clients is an indication of the degree of importance the industry attaches to the function. Such is based on the responses obtained regarding the protection of investors as the clients' of the stockbrokerage firms' by asking the respondents' whether the firms informed their clients on any significant corporate changes. One of ten firms does not inform its clients, while the rest do inform their clients with only one out of the remaining nine firms informing the clients before any changes take place. The firm's response from this question signifies that the opinion of the clients in making significant corporate changes doesn't count hence lack of incentive to effectively and efficiently inform the clients/investors on any corporate changes of investor.

The Kenyan stockbrokerage industry is characterized by lack of investor representation in the board and proper channels in safeguarding their interests. The question sought to determine

the operations of the firms in protecting the interests of clients but the respondents gave out answers containing structures that have been put in place, that is, two firms mentioned the in-house customer relations departments as the other firm highlighted the compliance with the rules and regulations, a factors which I wasn't able to determine whether true or false. On the practice of affording the clients basic rights by virtue of them being investors, 5 firms focused on equal access of information by all investors while out of the ten stating that they do practice a degree of disclosure and transparency to their clients. On this category only 3 firms out of the 10 recognized that they are obligated to provide services to their clients in an efficient and effective. Responses from this category of questions signified a very low percentage of the firms in the industry attaching any enforceable rights to their clients.

4.5 Interpretation and Discussion of Findings

4.5.1 Corporate Governance and Investor Protection in the Kenyan Stockbrokerage Industry

Current studies have indicated that the protection of investors goes a long way in enhancing the developments of a country's financial markets (La Porta, Lopez-De-Silanes, Shleifer and Vishny, 2002). Nevertheless even if required by the market regulator, it might be a difficult task to ascertain the compliance of such regulations seeking to protect investors. For example Bianchi, Ciavarella, Novembre and Signoretti (2010) asses the actual level of compliance for Italian listed firms and find out that the official levels of compliance declared by issuers is much higher than the actual levels of the firms compliance to the Italian corporate governance code. This observation might signify that the issuers might have resorted to the box-ticking approach in their declaration of compliance with corporate governance code. If that's the case then it would therefore not be a surprise to find out the same scenario in the Kenyan stockbrokerage industry as all the 10 firms surveyed indicated that to date, they have never been

fined by the market regulator for non-compliance of the corporate governance rules and regulations.

The fact that the member firms of the Kenyan stockbrokerage industry are conscious of the importance of taking into account the interests of different stakeholders especially their client's interests might not signify that they do indeed apply such knowledge. This may well be evidenced by the fact that the firms do not have any of their clients' representatives sitting in their boards nor do they have any structures establishing and enforcing the basic rights of their clients over their interests in the company, that is, their investments. And with such a scenario the practice of good governance in the stockbrokerage industry would be would be clouded in uncertainty considering that it has been observed by authors such as Cingula (2006), that good corporate governance practice relates to the control of business activities of a firm while at the same time promoting a dependable relationship between the owners and different stakeholders.

Remarkably, majority of the number firms of the stockbrokerage industry were of the opinion that a balance of the interests of both their external and internal stakeholders is requisite for good corporate governance. According to Mescher (2011) this is possible. Nevertheless in practice this doesn't happen as observed by Greenfield (2008) that in cases where the executives in charge of a firm adopt a broad outlook to consider the interests of different stakeholders and communities neighboring the firm, such executive/s are usually viewed as an underperformer and at times criticized for digressing from the interests of the shareholders. The author calls for firms to considerably take into account the interests of different of its stakeholders stating that such a move will translate to it to adopting strategies and decisions for the long-run well-being of the firms, an observation that can benefit the Kenyan stockbrokerage firms and its shareholders.

On the enforcement of stakeholders' interests, Greenfield (2008) brings to the fore ethical concerns in balancing stakeholders and shareholders' interests in a corporate set-up. The author illustrates that in the event where a company executive lies to the shareholders of the company in a shareholders meeting, the executive might have at that point committed a crime with dire consequences. The author then states that this would not have been the case if the executive were to lie to the employees in a company meeting. The author finally points out that ethical business practice doesn't only mean compliance with the laws and regulations, but also making sure that the governance of the company make allowances for the different concerns that the company has influence over. This is the position that did not clearly come out in the study as it was noted that most firms were concerned with regulatory compliance rather than voluntary ethical practices most probably due to the repercussions of non-compliance. If this was not the case then the firms would for instance clearly spell out the international corporate governance principles they declared they embraced in their practice of corporate governance.

The local corporate governance framework which mainly consists of the companies Act Cap 486 of the laws of Kenya and the Capital Markets (Corporate Governance) (Market Intermediaries) regulations, 2011 have not to date been able to come out strong enough to assert stakeholder focus in the practices of corporate governance. In fact most of the companies that embrace stakeholder interests do so in form of corporate social responsibility while others for marketing and public image purposes. From the response of the stockbrokerage firms with regards to their practice of corporate governance, it can then be observed that the protection of the welfare of investors still doesn't count among their key priorities in the practice of corporate governance. This observation stems from the fact that two firms out of the ten that were surveyed responded that they complied with only the local regulatory framework which mainly focus on

the protection of shareholder interest from misappropriation while the rest of the eight firms claimed that they do follow international standards of corporate governance but they were unable to exactly point out which international standards such as the Organization for Economic Co-operation and Development (OECD) principles of corporate governance that actually factors in the interests of different stakeholders in the practice of corporate governance.

Striking a balance between the interests of the owners of wealth , that is, the shareholders as well as the different stakeholders of the corporate entities is possible. This is highlighted by Rose and Mejer (2003) who stated that the corporate governance practices of the Danish firms traditionally focused more on the interests of diverse stakeholders. The authors then point out that recently more emphasis has been directed towards promoting shareholder value without any actual effect to the market initiatives in protecting the interests of diverse stakeholders. Okpara (2011) examines the corporate governance constraints in Nigeria and highlights a study by the Center for International Private Enterprise (CIPE) and the Institute of Economic Affairs (IEA) in 2001 which pointed out stakeholder ignorance as part of the constraints in the promotion of good governance in Nigeria. Ignorance is particularly attributed to lack of sufficient knowledge with regards to a specific issue. Therefore might this be the same case with the Kenyan stockbrokerage industry? The firms surveyed totally declined to respond to the question on how they would ensure that their clients access crucial information in a timely manner. Furthermore, owing to the fact that the clients of the stockbrokerage firms are informed on corporate changes after they take place brings out concerns on the level of ignorance prevalent on protection of investor interests by the Kenyan stockbrokerage industry.

4.5.2 Corporate Governance and Ownership Concentration in Kenyan Stockbrokerage Industry

Fan and Wong (2002) investigated the relationship between earnings informativeness and ownership structure of 977 firms in the East Asian economies and came to the conclusion that concentrated ownership and allied structures bring about agency conflict between the controlling owners and the external investors. Additionally, the authors found out that the controlling shareholder are bound to disclose firm accounting information that lacks credibility to external investors due to the fact that such disclosure of accounting information is done for self-interest purposes. The authors also observed that such concentrated ownership limits the outflow of a firms' rent seeking activities hence associated with low price informativeness. This study paints a very grim picture for the Kenyan stock brokerage industry which is highly concentrated. Out of the ten firms surveyed, two firms were wholly owned by a family , that is, 100 percent family owned.

Apart from family owned concentration, a prevalent characteristic in the ownership of the firms constituting the Kenyan stockbrokerage industry is the institutional shareholding with four firms out of the ten surveyed having institutional shareholders. Each of these four firms is surprisingly 70 percent or more owned by institutional shareholders. This is quite a precarious position considering studies have overtime indicated the perils of concentrated ownership and especially in the case where the industry in question is the stockbrokerage industry. Faroughi and Fooladi (2012) investigate the relationship between ownership concentration and firms performance of the firms listed in the Tehran Stock Exchange and found out that firms performance is negatively related to ownership concentration and particularly highlighted that ownership concentration impacts the performance of differently based on the industry. From

their study, the authors concluded that operational and financial risks together with resource expropriation are some of the consequences of high concentration of ownership.

Abdoli and Pourkazemi (2012) examined the effects of corporate governance components on bankruptcy between 2008 and 2010 of 95 firms listed in the Tehran Stock Exchange and concluded that there is an existence of a positive relationship between ownership concentration and corporate bankruptcy. These results are quite analogous to the situation in the Kenyan stockbrokerage industry which has always been highly concentrated and has had its share of misfortunes with four stock stockbrokerage firms from collapsing within a three year period. This scenario is also not quite different from Pakistan where a study conducted between 2006 and 2010 of forty firms listed in the Karachi Stock Exchange found out an increase in ownership concentration negatively impacts the practices of corporate governance within the firm (Shah and Kouser 2012). Reiterating the same, Lskavyan and Spatareanu (2006) studied the relationship between ownership concentration and performance in public traded companies in UK, Czech republic and Poland and reached to the conclusion that ownership concentration is insignificant to firm performance both in cases where there is weak market monitoring in the case of Czech and Poland as well as where market monitoring is strong.

In a bid to examine family ownership and control of large firms, Peng and Jiang (2010) collected data from 634 publicly listed companies in Hong Kong, Indonesia, Malaysia, Singapore, South Korea, Taiwan and Thailand. Their study found out that the benefits of family controlled firms in countries with more developed institutions outweigh the costs. The study particularly pointed out that better internal control mechanisms and better access to resources as benefits of having a family CEO in more developed institutions. Nevertheless expropriation of minority shareholders was observed to be as a result of having family controlled firms in less

developed institutions. Using a sample of 434 firms listed in the Bursa Malaysia between the years 1999 and 2000, (Wahab, How and Verhoeven, 2008) and come to the conclusion that the positive relationship between corporate governance and institutional ownership declined more after the year 2001.This was the year that the Malaysian Code of Corporate Governance (MCCG) was incorporated into the Kuala Lumpur Stock Exchange (KLSE) listing rules. The 2001 corporate governance reforms had the effect of heightening institutional shareholder activism in the listed firms. More studies continue to highlight the confronts of ownership concentration with some mentioning principal to principal conflicts between the controlling shareholders and the minority shareholders (Young et al, 2008) and the expropriation of minority shareholders by the controlling shareholders (Claessens and Fan, 2002).

CHAPTER FIVE

CONCLUSION AND RECOMMENDATIONS

5.1 The Significance of Good Corporate Governance Practice on Firm Performance

The collapse of the four stockbrokerage firms between 2006 and 2010 and the subsequent loss of the funds of their clients raised a lot of questions on the ethical standards and practices in the Kenyan stockbrokerage industry. More so concerns on the mechanisms put in place to safeguard the interests and affairs of these investors/ clients emerged. Taking everything surrounding the debacle in to consideration, one a factor that is still uncertain is the cause of the collapse of the firms. Nevertheless what is clear is that the mismanagement of the investors' funds by these institutions which were supposed to be intermediaries pointed to the lack of clarity in transparency in the governance practices of these firms. Hence the need for precise information regarding the corporate governance practices of these institutions and the entire Kenyan Stockbrokerage industry that is if accessible, would enlighten the general public, both the current and potential clients of the Kenyan stockbrokerage industry, as well as effectively informing the securities market regulator.

Transparency and disclosure is a crucial component of contemporary practice of contemporary corporate governance. However do corporate governance reforms on the transparency and disclosure mechanisms actually affect firm performance? Kuznecovs and Pal (2012), sought to examine this by using data from Russia over 2000 to 2008 and arrived to the conclusion that instituting such reforms had minimal effect on firm performance. The author pointed out that this might have been due to the acquisitive nature of the central and local governments where the central government aggressive tax enforcement makes firms shy away

from augmenting their transparency and disclosure practices, while sheer malfeasance exerted by the decentralized local governments officials in form of bribes with a promise to reprieve the business from the high taxes levied by the central government eventually impending the performance of the firms.

Over time scholarly research has been able to point towards the existence of a relationship between corporate governance practice and the performance of a firm. For instance, using a sample of 310 large Australian companies, Hutchinson and Gul (2004), investigated whether corporate governance subdues the negative relationship between a firm's growth opportunity and firm performance and come to a conclusion that corporate governance plays a crucial role in the performance of companies. Echoing the same Khatab, et al. (2011), used data from the annual report for the years 2001 to 2003 of twenty firms listed at the Karachi Stock Exchange to investigate the relationship between corporate governance and firm performance. The outcome of the study indicated that companies having good corporate governance practices outperform those companies without any or having partial good corporate governance practices. Both of these studies indicated the positive relationship between the practice of good corporate governance and the performance of firms.

What's more, in seeking to answer the question on whether there is an actual relationship between corporate governance and firm performance, Chaghadari (2001), highlights the primary purpose of corporate governance, that is, to align the interests of different stakeholders of a firm with the goals of executive of the firms. In this study, the author used a sample of randomly selected companies listed in the Bursa Malaysia to investigate the relationship between firm performance as a dependent variable and board independency, CEO duality, ownership structure as well as board size as independent variables. The study found out that CEO duality has a

negative relationship with firm performance while the rest of the three remaining independent variableness did not have a significant relationship with the firm performance. Importantly, the proficiency of the board of directors in exercising its role of monitoring the exploits of executive is suppressed in the cases where the Chief Executive Officer is also the chair of the board and hence poor monitoring and control of the firms' executive by such boards of directors.

Various studies from across the globe have called for the inclusion of external independent directors in the board of directors solely for the function of bolstering the monitoring and control role of the boards. Such significance of external independent directors as a good corporate governance measure on firm value and firm performance was evaluated using a sample of 157 non-financial Indian companies in 2008 (Kumar and Singh, 2012). The study found out that external independent directors have a positive but an insignificant effect on firm value. Similarly Javed and Iqbal (2006), examined the relationship between corporate governance and firm performance using a sample of 50 firms listed in the Karachi Stock Exchange. With a large percentage of firms listed in the bourse either being family or institution owned, the authors point out that it's important for external independent directors to be included in the boards of such companies since the ownership and control of the firms is closely aligned. Despite the study showing significant relationship between the performance of the firms and the quality of firm level corporate governance, good corporate governance practice of open and transparent disclosure of relevant information in a bid to trim down information asymmetry was observed to having no effect on the performance of firms.

On a side note, firms having weak governance structures have been observed to exhibit inordinate agency problems which in turn translates to poor performance (Core et al., 1999). In a bid to enrich the governance structures of firms and enhance the role boards of directors in

monitoring the activities of the management, economies such as Korea brought about changes in the country's corporate governance framework after the Asian financial crisis (Choi et al., 2007). These changes which among others required listed firms to have a minimum of 25 % of outside directors were primarily driven by the International Monetary Fund (IMF) and shareholder activism. The results of such changes were observed to have had a positive and significant effect in the performance of the firms especially in cases where the outside directors were independent directors rather than gray directors. In this case, gray directors are external non-executive, non-independent director's, that is, external directors who are not independent since they are associated with either the executive directors or the shareholders of the firm. Nevertheless

On the same note, Fauziah, Yusoff and Alhaji, (2012), use a sample of 813 firm listed in the Bursa Malaysia over 2009 to 2011 to investigate the relationship between corporate governance and firm performance. The authors based their study on three major corporate governance components, that is, the proportion of non-executive directors in the boards of the companies, the board leadership structure, and the size of the boards of directors. The outcome of the study indicated that the presence of independent directors and the size of the board as components of corporate governance significantly impact the performance of the firms. In particular, the results indicated that the presence of independent directors in the board positively influences the boards' decision making process as well as its management monitoring ability ultimately enhancing the ability of the board to attend to issues pertaining to the overall performance of the company. Francis et al. (2012), equally investigated whether and to what extent the boards of directors influence the performance of firms using cumulative stock returns during the contemporary financial crisis. And similar to the findings of the study by Fauziah, Yusoff and Alhaji, (2012), the study found out that it is only the independent directors who are

not connected with the management of the company in any, that is, external independent directors who positively and significantly impact the performance of firms during the crisis.

Regarding the structure of the board of directors as an important component of corporate governance Guest (2009), investigates the bearing of the size of the board on the performance of a firm using a sample of 2746 United Kingdom listed over 1981 to 2002. The study finds that board size has a negative impact on the performance of a firm with the findings advancing the case for a small size of board of directors in lieu of large boards which have been associated by numerous scholars with poor communications second rate decision making. In a similar study, Velnampy (2013), used a sample of 28 Sri Lankan manufacturing firm during the period of 2007-2011 to investigate the impact of corporate governance on firm performance. The study focuses on board structure, board committees, board meeting, and board size as the elements of corporate governance while firm performance being measured using returns on equity (ROE) and returns on assets (ROA). The results of the study revealed that the corporate governance elements employed did not have an effect on the firm performance measures of returns on equity and returns on assets. Based on the outcome of the study the author urged firms to constitute board of directors having more independent directors in order to boost their executive monitoring role effectiveness. Nevertheless, Achchuthan and Kajananthan (2013) arrived to a dissimilar observation in their study which indicated the examined corporate governance practices of board leadership structure, board meetings, and proportion of non-executive directors had no significant effect in firm performance. The study sought to find whether there is a distinction between the corporate governance practices on firm performance by sampling 28 manufacturing firms listed in the Colombo Stock Exchange over 2007 to 2011.

Bhagat and Bolton (2008), recommend that seeing as corporate governance is positively associated to future operating performance as well as the probability of disciplinary management turnover in firms performing below par, and then the endeavours to better corporate governance should be directed towards stock ownership of board members. The authors examined the inter-relationship between corporate governance corporate performance, corporate capital structure and corporate ownership structure in a bid to expound on the relationship between corporate governance and firm performance. However the recommendations of the study as a corporate governance mechanism might not bring in any positive change in the current Kenyan stockbrokerage industry. From the results of this study it is evident that virtually all of the board members of the firms in the entire industry are either stockholders or are there to represent the interests of the shareholders of the firms. At their point though, a sound strategy such a move might not be able to work at observed by the authors.

5.2 Recommendations

Tornyeva and Wereko (2012) observe that good corporate governance not only safeguards the interest of the firm's stakeholders by aligning their interests with that of the executives but also augments transparency of firm's operations, ensures accountability and advances the firm's profitability. The results of their study particularly indicated that there is a positive relationship between the financial performance of insurance companies in Ghana and large board size, board skill, management skill, longer serving CEOs, size of audit committees, audit committee independence, foreign ownership, institutional ownership, dividend policy, and annual general meetings as corporate governance elements. Their study sought to assess the relationship between corporate governance and financial performance of insurance companies in

Ghana determined that firm profitability is positively influenced by corporate governance. Tabără, and Ungureanu (2012), also arrived at the same observation determining that firms with good corporate governance practices have the potential to augment their overall performance. The authors articulate that such a positive relationship stems from the fact that with good corporate governance practices, firms willingly disclose distinct information on their operations and status to the public which increases investors confidence in such firms thereby positively affecting the market valuation of the firms and eventually increasing the prices of the firms stocks in the securities markets and consequently business value.

The benefits of practicing good corporate governance have therefore never been in contention and more so in volatile industries such as the stockbrokerage industry. The Kenyan stockbrokerage industry has not been an exception to the business failures which resulted to the loss of magnitude of investments by innocent investors. Since most studies have proven that corporate governance practices are related to firm performance, this study sought to bring to light the corporate governance practices of the Kenya stockbrokerage industry, focusing on two core determinants of corporate governance , that is, the ownership structures and the investor protection initiatives of the member firms. With ten firms out of the eleven present in the industry having been surveyed, it can be therefore construed with certainty that the outcome of the study represents a fair picture of the corporate governance practices prevailing in the stockbrokerage industry in Kenya.

5.2.1 The Kenyan Stockbrokerage Industry

A major concern that was brought out by the study lies with the effectiveness of the mode of communicating or passing investment related information to the clients of the stockbrokerage firms. The mode of communication should be consistent, timely and effective in passing

essential information to the recipient. The member firms in the Kenyan stockbrokerage industry need to enhance the means and effectiveness of the communication of the investment by not only improving the transparency of their activities with regards to how they handle the investments/ funds of their clients but they should do it in a timely manner and with the most effective way that would ensure the information gets to the client at the earliest time possible. Client engagement should be timely and effective be able available all the clients without regard to their size of their investments. Possibly the firms can profile their clients by identifying the needs of each of their clients and the most preferred form of communication. And on the some note, the firms can also build-up on embracing technology in passing such crucial information to their clients such as using mobile phones (text message updates) and at times through their clients e-mail address. This will go a long way in ensuring that investors become active in monitoring their investments.

The stockbrokerage firms should also endeavour to regularly educate their personnel on the current good corporate governance practices. These practices should mainly revolve around the rights of the different stakeholders of the firms and more so the investors/clients. Such training should additionally focus on the identified contemporary issues affecting the whole industry for instance, the disseminating of information to the clients of the firms and the fair treatment of the different types of investors/ clients. It is also recommended that among the good corporate governance practices to be embraced by the firms in the industry is to have a substantial number of external independent directors on their boards probably representing the interest of the investors more so the minority/small scale clients who from this study were noted to be marginalized in information dissemination together with other benefits enjoyed by the large scale/ institutional investors. Such inclusion of external independent directors in the boards of the

firms will go a long way in enhancing the monitoring of the management undertakings while at the same time ensuring that the diverse interests of the different stakeholders of the firms are well taken into account.

5.2.2 The Capital Markets Authority (the Kenyan securities markets regulator)

The Kenyan Capital Markets Authority (CMA) as the securities markets regulator and the licensing authority of the stockbrokerage firms ought to develop a more stringent regulatory framework that effectively addresses high risk issues in the Kenyan stockbrokerage industry such as the ownership structures of the stockbrokerage firms. As identified by the study, the Kenyan stockbrokerage industry has a highly concentrated ownership structure with some of the member firms being owned by institutions or families with holdings in more than 70% (seventy percent). Such concentrated ownership is highly risky as it makes easier for the controlling shareholder(s) to take advantage of their influence in the control of the firm to serve his/ her selfish interests to the detriment of the employees, the clients and if any, other shareholders. The regulatory framework should therefore call for a well structured and diversified ownership of the firms in the industry in order to address this particular pressing issue.

The market regulator should also endeavour to come up with regulatory framework that will enhance the monitoring and control of the stockbrokerage firms. Since the role of monitoring and control of a firms executives lies with the board of directors which is also the ultimate decision making organ of the company, the markets regulators' regulatory framework reforms targeting the stockbrokerage industry should begin by addressing the structure and role of the boards' of directors. In this case, it is particularly recommended that Capital Markets Authority makes necessary changes to the regulatory framework that would oblige the stockbrokerage firms to have a substantial number of external independent directors sitting on

their boards. Research has already proven that the presence of external independent directors in the boards boosts the boards monitoring and control role and thereby positively affecting the performance of such firms. Such external independent directors should be absolutely independent, that is, not connected or associated with the firms' executive officers or the internal board of directors and should also have within them members representing the minority/ small scale investors.

The presence of stringent laws without being accompanied by severe sanctions for non-compliance will not be very effective as potential perpetrators usually weigh the benefits of non-compliance against the sanctions they stand to face in case they get caught and if the benefits outweigh the sanctions, the perpetrators will proceed to break the laws without taking any slight interest on the repercussions of the actions. Furthermore, the force of stringent laws and severe sanctions can be watered down if laxity in law/ regulatory enforcement is observed. In this case, even where the sanctions from breaking the laws/ regulations outweigh benefits derived from such action, the perpetrators will go ahead to break the law since they will be aware that the chances of them getting away with the particular offence is very high. It is therefore imperative that the Capital Markets Authority formulates regulations with severe sanctions backed up by thorough and aggressive enforcement that would scare-off any potential perpetrators. Additionally it is recommended that the Capital Markets Authority ought to aggressively monitor the compliance of their regulations by the member firms of the Kenyan stockbrokerage industry. This will ensure that the perpetrators who have failed to comply with the required laws and regulations are promptly detected. Strict monitoring and prompt detection of firms that have failed to comply with the regulations will go along away in boosting the compliance of the regulations. It is also proposed that additional measures be put a place to create a channel where

investors can report any suspicious activities by the firms handling their funds, regulatory non-compliance, and infringement of their rights by the firms.

In exercising its regulatory making powers, the Capital Markets Authority should formulate regulations that would make it mandatory for both executives and employees of the stockbrokerage firms to undergo regular training followed by an assessment on the contemporary corporate governance practices specifically designed for the stockbrokerage industry. The corporate governance practices should be coded in the regulatory framework of the Capital Markets Authority and should encompass measures that have been identified as risks and/ or shortfalls that resulted in the collapse of the stockbrokerage firms. This will in turn strengthen the regulatory enforcement role and at the same time ease the market regulators monitoring of the stockbrokerage industry. All in all regulatory reforms the Kenyan stockbrokerage industry should mainly focus on the structure of the boards of directors of the member firms, the ownership structure and ultimately client/ investor protection initiatives.

5.2.3 The Clients (Investors) of the Kenyan Stockbrokerage Firms

The findings of this study indicate that there is a dearth of good corporate governance practices in the Kenyan stockbrokerage industry more so, practices aimed at protecting the interests of the investors/clients of the member firms. The consequence of such omission being that investors especially the small scale/ minority are pushed in the background and disregarded while the firms focus on maximizing the stockholders wealth. In this scenario, the investors (in most cases the institutional and large scale investors) who have potential of expanding the fortune of the stockholders and the executive are given undivided attention. With this in mind, the study therefore recommends that the Kenyan securities market regulator ought to carry out an investors sensitization programme whereby all the clients/investors will be informed of their

rights as clients of the stockbrokerage firms, the obligations owed to them by the stockbrokerage firms and the importance of as well as how they can actively monitor the management of their investment and the performance of the firms. The client/investors of the stockbrokerage firms should be encouraged and supported in their efforts to proactively question the company's activity(ies) where necessary and to promptly report any suspicious activities to the Capital Market Authority accordingly.

5.3 Conclusion

The study has profoundly examined the corporate governance practices of the member firms of the Kenyan stockbrokerage industry. The study focused on two core corporate governance determinants as independent variables, to be precise, the ownership structures of the firms and the client/investor protection initiatives. From the primary objectives of the study, the corporate governance practices of the Kenyan stockbrokerage were examined in light of the collapse of the four stockbrokerage firms operating in the Nairobi Securities Exchange between 2006 and 2010. The study focused on the mainstream stockbrokerage firms licensed by the Kenyan capital market authority bringing to light the corporate governance practices of ten firms and therefore making the findings of this study to represent a fair picture of the practice of corporate governance relating to the two core elements. Importantly the findings of this study bring to light the precarious status of corporate governance practices in the Kenyan stockbrokerage industry.

The findings of this study indicate that the Kenyan stockbrokerage industry is plagued by infinitesimal comprehension of the works and benefits of good corporate governance. Most employees would shy away from responding to certain questions which can be interpreted that either the employees do not have a grasp of the basic tenets of corporate governance or if not,

then they were not comfortable disclosing certain aspect of their firms corporate governance practices. This might also be interpreted that most firms are focused on regulatory compliance possibly due to the fear of the repercussions of non-compliance rather than complying with the corporate governance codes for the benefit of the firms and its different stakeholders. This is an unpleasant picture of the industry with regards to its corporate governance practice especially since the Kenyan stockbrokerage is still growing and would definitely benefit from prioritizing on good corporate governance practices.

The risk levels of the general industry as painted by the findings of the study are very high since minority/ small scale clients of the firms are disregarded in a number of cases with most attention being accorded to the large scale investors. This is not withstanding the fact that the small scale investors it put together, account for a large share of investment holdings in the firms. Another risk factor in the Kenya stockbrokerage industry brought out by the findings is the concentrated ownership prevalent in the ownership structures of the firms which makes the firms vulnerable to abuse by the controlling shareholders. Finally the outcome of this study has significant implications on the measures engineered by the Kenyan Capital Markets Authority, the Nairobi Securities Exchange and investors generally in: (i) devising an effective model for the structure of the board of directors of the member firms of the Kenyan stockbrokerage industry; (ii) devising an appropriate ownership structure model for the Kenyan stockbrokerage industry that addresses high risk issues in the industry such as ownership concentration and insider control; and (iii) devising an investor sensitization programme for the clients of the stockbrokerage firms as well as a training module targeting the employees, the directors and the executives of stockbrokerage firms that word ensure investors engagement as well as a positive reception of good corporate governance practices in the industry respectively. In the course of

the study concerns on the causes of the collapse of the stockbrokerage firms between 2006 and 2010 were raised. It is therefore suggested that future research addresses this vital issue. Additionally, future research can consider the different elements of corporate governance practices apart from ownership structure and investor protection which are comprehensively covered by this study.

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