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## **The Effects of Ownership Structure on Financial Performance of Unit Trusts in Kenya**

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### **Abstract:**

*Unit trust fund is a form of investment where many investors with similar investment objectives pool money together to be managed by a group of professional managers who invest the pooled money in a portfolio of securities such as shares, bonds and money market instruments or other authorized securities. The concept has been adopted in the Kenyan markets and by 2009, there were 11 operational unit trust funds. However, performance of unit trusts in Kenya in the recent past has witnessed relatively poor results characterized by financial results falling below desired targets. Besides that, the unit trusts have been characterized by highly concentrated ownership, low ownership share of foreign owners, high ownership and decision making power in the hands of the state owned and relatively low ownership shares in the hands of insiders. This trend has continued despite the regulations enacted by Capital Markets Authority to provide a framework for the regulation of collective investment schemes to protect shareholder investment and maximize returns. This study aimed was designed to establish how ownership structure affects financial performance of the Unit Trusts in Kenya. The study investigated 11 unit trust funds in Kenya. The target population comprised of all the 11 fund managers in the registered Unit Trusts in Kenya. Secondary data on performance of the unit trusts and primary data from managers of unit trusts were utilized. Data was analyzed using descriptive statistics which included: mean, mode standard deviation frequencies and percentages. Further relationships were obtained between independent and dependent variables using Pearson Product Moment Correlation (R). The findings revealed that diversity in ownership structure of unit trusts to positively affected financial performance among unit trusts. The study, therefore recommended for improvement in management style, increase investment portfolios and diversify asset investment among the unit trusts strategy to realize meaningful stability in financial performance.*

**Keywords:** Unit Trust, Financial Performance, Ownership

### **1. Introduction**

A unit trust fund is an investment scheme that pools money together from many investors who share the same financial objective. The funds are managed by a group of professional managers who invest the pooled funds in a portfolio of securities such as shares, bonds and money market instruments or other authorized securities to achieve the objectives of the fund (Capital Markets Authority, 2010). The funds are collectively invested in a portfolio of assets such as shares, bonds, money market instruments and other authorized securities, in line with the common objective and needs of the group of investors. The Kenyan capital markets offer an array of investment products which include shares, bonds and unit trusts. In Kenya, the Unit trusts play a pivotal role in the growth and development of the Kenyan economy with an average annual growth of 1.9 billion. Unit trusts have grown in acceptance and popularity in recent years evidenced from growth of unit trust funds from virtually zero in 2001 to 11 in 2008 (Capital Markets Authority, 2010).

#### *1.1. Statement of the Problem*

Unit trusts in Kenya have grown at an average of Sh1.9 billion annually to Sh17.6 billion in the past nine years, much slower than other financial sector investments such as pensions funds (CMA, 2010). However, the factors responsible for the poor performance of unit trusts in Kenya have not been documented. Much of the literature on the performance of organizations in Kenya is centered on how institutional investors affect the performance of corporations (Illig, 2008; Alsaeed, 2006). Little attention has been paid by scholars in examining the effects of organizational factors on the performance of unit trusts. In view of this gap in knowledge, the study examined the effects of ownership structure of unit trusts on their performance.

### 1.2. Objective of the Study

To establish how ownership structure affects financial performance of the Unit Trusts in Kenya

### 1.3. Hypothesis

- $H_0$ : Ownership structure does not significantly affect Unit Trusts' financial performance in Kenya
- $H_1$ : Ownership structure significantly affect Unit Trusts' financial performance in Kenya.

### 1.4. Scope of the Study

This study was carried out in all the 11 registered Unit Trusts' of Kenya (Capital Markets Authority, 2009). It covered the fund managers and portfolio managers. The study was confined to examining the effects of organizational factors on performance of unit trusts in Kenya.

## 2. Research Methodology

### 2.1. Research Design

The study employed correlation research design. This design was considered appropriate since the purpose of this study was to establish if a relationship exists between the independent variable (ownership structure) and dependent variable (unit trusts' financial performance). The study has a cause – effect orientation and therefore, the discovery of association would suggest the possibility of 'cause', that is, while the fact that the independent and dependent variables are correlated does not allow us to directly infer causation but if the variables are causally related, they must be correlated.

### 2.2. Study Population

The target population comprised of all fund managers and Portfolio managers in the 11 registered Unit Trusts in Kenya. The study used portfolio and fund managers because they are strategically placed to provide the required information. A total of 44 managers were targeted, comprising of 11 fund managers, and 33 portfolio managers. Census approach was employed in selecting all to participate.

### 2.3. Data Collection Method and Instruments

The study used a data collection sheet to collect secondary data from and questionnaire containing both structured and unstructured questions to gather primary data from unit trust managers of selected unit trusts.

### 2.4. Data Analysis and Presentation

Data collected was edited, coded, classified with regard to the type and source and keyed into SPSS spreadsheets. Data was analyzed using descriptive statistics which included: mean, mode standard deviation frequencies and percentages. Further relationships were obtained between independent and dependent variables using Pearson Product Moment Correlation (R) with the aid of the Statistical Package for Social Sciences (SPSS).

## 3. Findings

### 3.1. Characterization of Unit Trusts per Investment Portfolios per

Table 1 shows the characterization of nit trusts studied based on their investment portfolio

| Name of Trust            | Number of Investment Portfolios |
|--------------------------|---------------------------------|
| Standard Investment Bank | 3                               |
| CBA                      | 2                               |
| Old Mutual               | 5                               |
| Zimelle                  | 3                               |
| Dyer & Bliar             | 2                               |
| Britam                   | 4                               |
| Suntra                   | 3                               |
| ICEA                     | 4                               |
| African Alliance         | 4                               |
| <b>Total</b>             | <b>30</b>                       |

Table 1: Characterization of Unit Trusts per Investment Portfolios

### 3.2. Ownership of Unit Trusts in Kenya

Type of ownership of unit trust was categorized as either bank owned or non- banked, the findings are presented on Table 2:

| Response       | Frequency | Percentage |
|----------------|-----------|------------|
| Bank owned     | 2         | 22.2       |
| Non-bank owned | 7         | 77.8       |
| <b>Total</b>   | <b>9</b>  | <b>100</b> |

Table 2: Type of Ownership of Unit Trust

The findings revealed that 77.8% of the unit trusts were non- bank owned, while 22.2% were bank owned. This therefore puts the unit trust to a situation whereby they had diverse accounting and management approaches which definitely would impact differently on their financial performance. Bank owned unit trust were considered to be more organized, assuredly they had the capacity to identify and recruit qualified personnel , who could steer the organization to better heights.

3.3. Diversity in Ownership Structure

In the eleven (11) unit trusts managers were asked to indicate the diversity in ownership structure based on the distribution of unit trust holders on a five point scale as shown on Table 3.

| Statement   | Mean  | S.D   |
|---|-------|-------|
| Ownership of the unit trust is concentrated in the hands of different unit-holders. | 3.778 | 1.093 |

Table 3: Diversity in Ownership Structure

The study findings revealed that 77.8% of the respondents generally agreed that ownership of the unit trust was concentrated in the hands of different unit-holders whereas 22.2% disagreed. On average, diversification was rated high in a 5 point scale at Mean = 3.778, SD 1.093.

3.4. Financial Performance of Unit Trusts

The level of financial performance among unit trusts in Kenya was assessed based on secondary data from CMA for the financial years 2009-2011. The various aspects of performance included total asset value, Total liabilities, Net asset values, profits and ROCE.

3.4.1. Total Asset Value among Unit Trusts (2009-2011)

On the basis of Figure 1, the total asset value in the equity fund, balanced fund, fixed income and Kenya Shilling fund generally increased from the year 2009, reaching the highest value in 2010 and then decreased in the year 2011. It is also notable that total asset value for the East African fund was fairly constant during the period 2009-2011. However, total asset value of the money market fund was observed to have fallen sharply between 2009 and 2010 and then rose sharply between 2010-2011. It is evident that total asset value in most of the portfolios except money market fund generally increased between 2009-2010 and fell between 2010-2011.

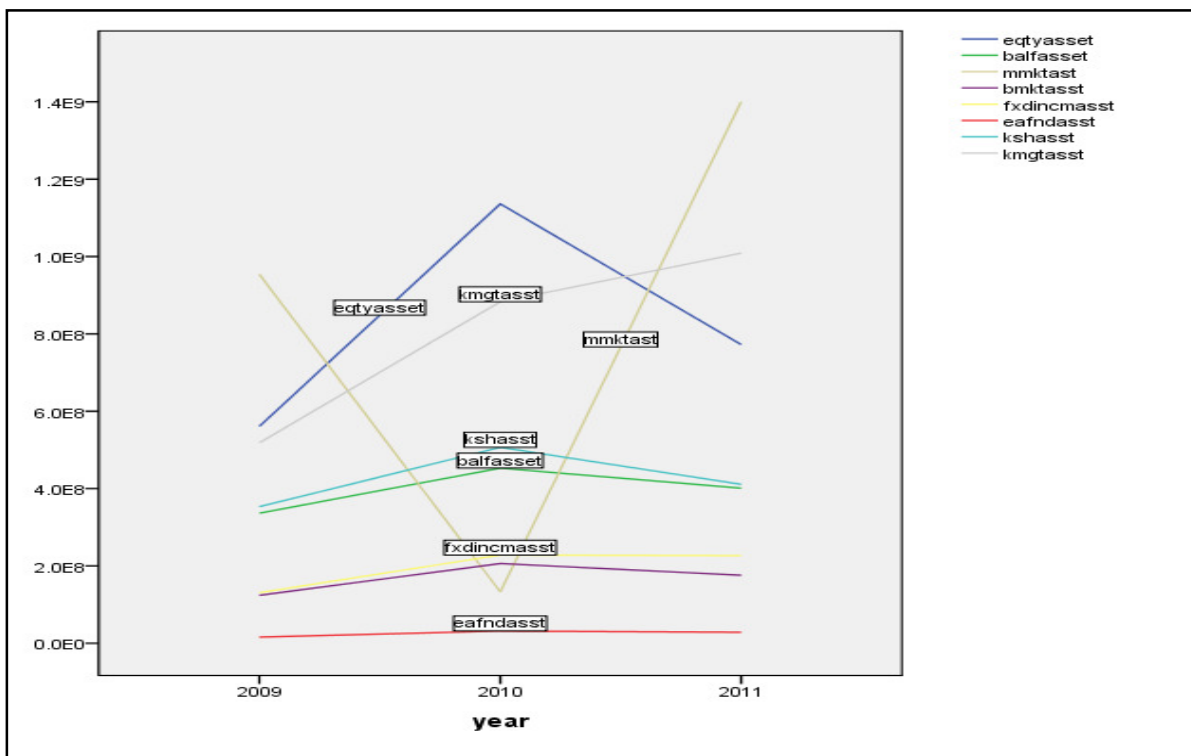


Figure 1: Total Asset Value (2009-2011)

3.4.2. Net Asset Value among Unit Trusts (2009-2011)

As shown on Figure 3 the total net asset value in the equity fund, money market fund, Kenya management fund, Kenya shilling fund, bond market fund and balanced fund generally increased from the year 2009, reaching the highest value in 2010 and then decreased in the year 2011. In addition, total net asset value for the East African fund was fairly constant during the period 2009-2011. Nevertheless, total net asset value of the fixed income fund was observed to have rose gradually reaching peak in 2010 and then remained fairly constant during the period between 2010-2011.

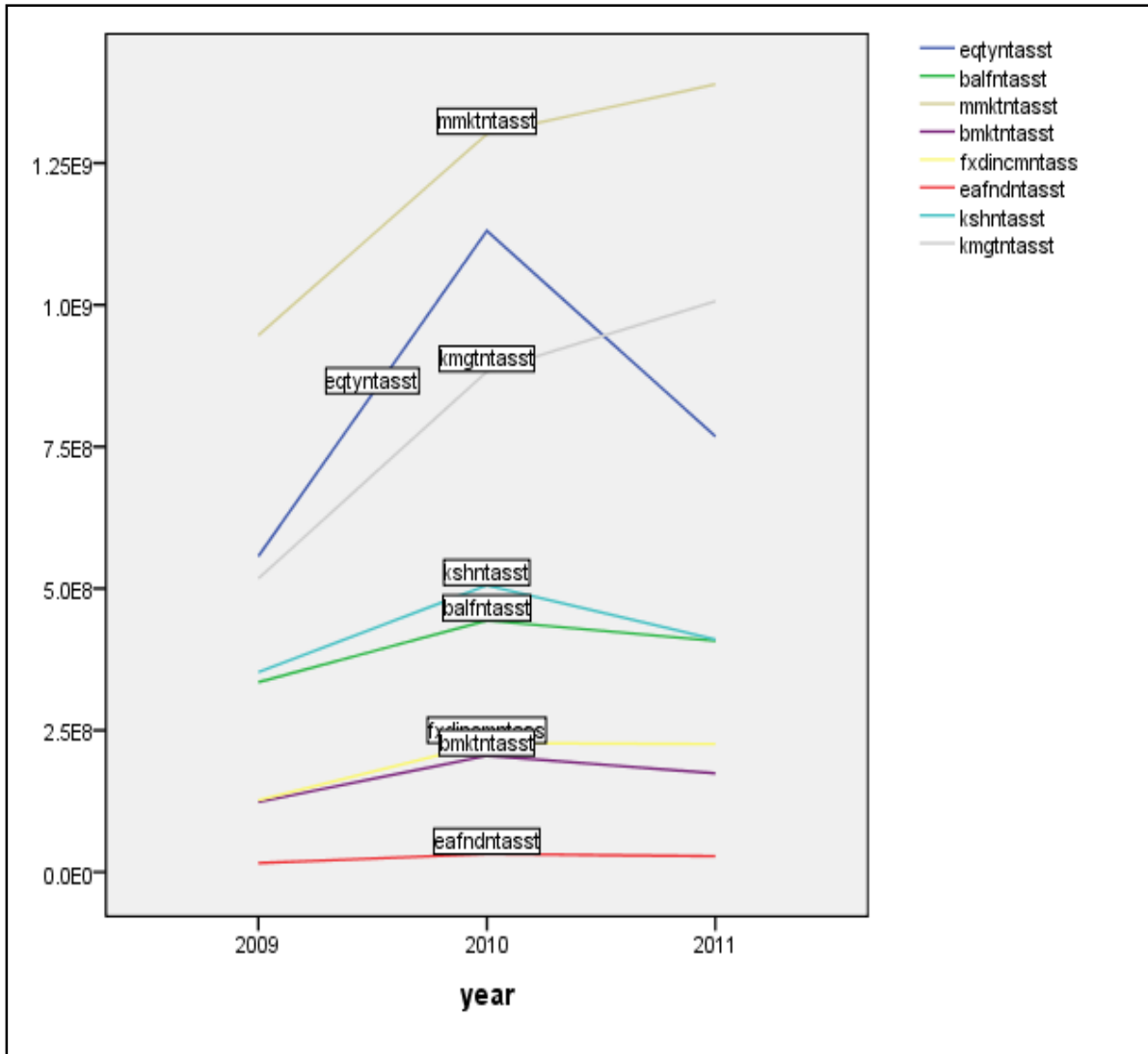


Figure 2: Total Net Asset Value (2009-2011)

3.4.3. Profits among Unit Trusts (2009-2011)

Based on the study findings on Figure 4, total profits in the equity fund and balanced fund experienced a sharp rise during 2009-2010 period, reaching peak in 2010 and then fell gradually during 2010-2011 period. It was further evident that the total profits in, Kenya management fund, Kenya shilling fund, bond market fund, fixed income fund and East African fund remained fairly constant during 2009-2011 period. It was also notable that the total profits of the money market fund was observed to have dropped gradually reaching its lowest in 2010 and then remained fairly constant during the period between 2010-2011. The general rise in performance could probably be associated with the recovery of the of the economy from the political crisis experienced in 2007-2008.

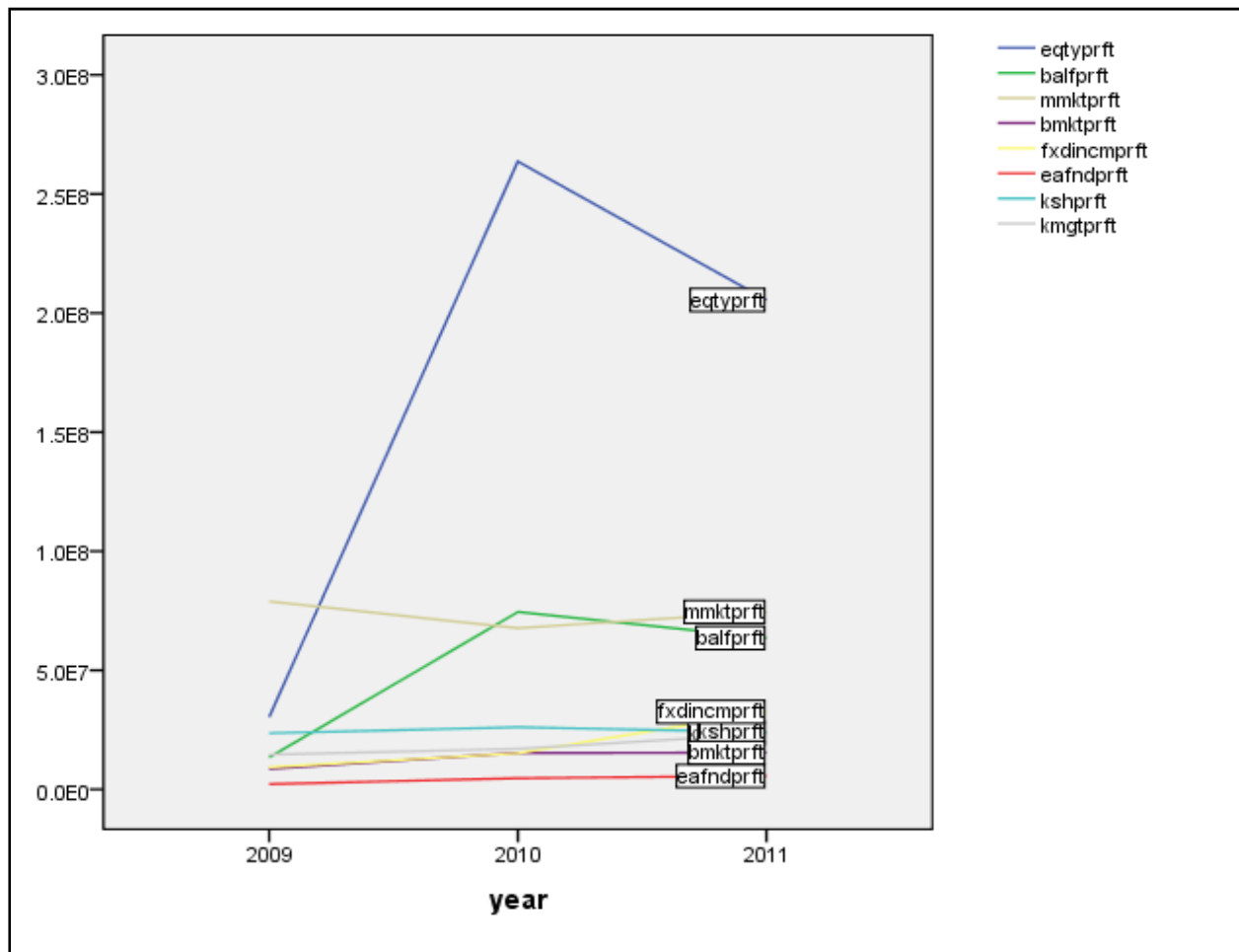


Figure 3: Total Profits (2009-2011)

3.4.4. Return on Capital Employed (ROCE) among Unit Trusts (2009-2011)

This was measured based on the Mean ROCE for the various investment portfolios in the trusts in Kenya.

| Trust                 | Mean ROCE |
|-----------------------|-----------|
| Equity Fund           | 14.9897   |
| Balanced Fund         | 10.3200   |
| Money Market Fund     | 4.6606    |
| Bond Market fund      | 10.1536   |
| Fixed Income Fund     | 7.1557    |
| East African Fund     | 16.5913   |
| Kenya Shilling Fund   | 5.8156    |
| Kenya Management Fund | 2.2817    |

Table 4: ROCE of Various Investment Portfolios in the Trusts

Study findings (Table 4.5.5) show that the mean ROCE values among the investment portfolios ranged between 2.2817 (lowest) and 16.5913 (highest). The East African fund (16.5913) and Equity Fund (14.9897) had the highest ROCE. The Balanced Fund, Bond Market fund, Fixed Income Fund, Kenya Shilling Fund had their ROCE as 10.3200, 10.1536, 7.1557 and 5.8156, respectively. It was noted that Money Market Fund and Kenya Management Fund and had the lowest ROCE (4.6606 and 2.2817, respectively).

3.5. Relationship between Ownership Structure and Financial Performance of Unit Trusts

The effects of ownership structure on performance of unit trusts in Kenya was computed by correlating the scores on diversity of ownership with profitability, ROCE and the Total Net Asset Value

| Profitability                      |                     |             |               |                   |                  |                   |                   |                     |                       |   |
|------------------------------------|---------------------|-------------|---------------|-------------------|------------------|-------------------|-------------------|---------------------|-----------------------|---|
| Organizational Ownership structure |                     | Equity Fund | Balanced Fund | Money market Fund | Bond Market fund | Fixed Income Fund | East African fund | Kenya Shilling Fund | Kenya Management Fund |   |
|                                    | Pearson Correlation | 0.411       | 0.994         | -                 | -                | -                 | -                 | -                   | -                     | - |
|                                    | Sig. (2-tailed)     | 0.360       | 0.001         | -                 | -                | -                 | -                 | -                   | -                     | - |

Table 5: Pearson Correlation between Ownership Structure and Total Profits

According to the test results on Table 5 organizational ownership structure was found to be positively associated to profits of the equity fund portfolio ( $r = 0.411$ ,  $p > 0.05$ ) and balanced fund portfolio ( $r = 0.994$ ,  $p < 0.05$ ).

| Return on Capital Employed (ROCE)  |                     |             |               |                   |                  |                   |                   |                     |                       |   |
|------------------------------------|---------------------|-------------|---------------|-------------------|------------------|-------------------|-------------------|---------------------|-----------------------|---|
| Organizational Ownership structure |                     | Equity Fund | Balanced Fund | Money market Fund | Bond Market fund | Fixed Income Fund | East African fund | Kenya Shilling Fund | Kenya Management Fund |   |
|                                    | Pearson Correlation | - 0.115     | 0.831         | 0.839             | -                | -                 | -                 | -                   | -                     | - |
|                                    | Sig. (2-tailed)     | 0.807       | 0.081         | 0.037             | -                | -                 | -                 | -                   | -                     | - |

Table 6: Pearson Correlation between Ownership Structure and ROCE

Pearson correlation results on table 6 show that organizational ownership structure was found to be negatively associated to ROCE of the equity fund portfolio ( $r = -0.115$ ,  $p > 0.05$ ) but positively associated to ROCE of the balanced fund portfolio ( $r = 0.831$ ,  $p > 0.05$ ) and the money market fund portfolio ( $r = 0.839$ ,  $p > 0.05$ ).

| Total Net Asset Values             |                     |             |               |                   |                  |                   |                   |                     |                       |   |
|------------------------------------|---------------------|-------------|---------------|-------------------|------------------|-------------------|-------------------|---------------------|-----------------------|---|
| Organizational Ownership structure |                     | Equity Fund | Balanced Fund | Money market Fund | Bond Market fund | Fixed Income Fund | East African fund | Kenya Shilling Fund | Kenya Management Fund |   |
|                                    | Pearson Correlation | 0.353       | 0.940**       | 0.877*            | -                | -                 | -                 | -                   | -                     | - |
|                                    | Sig. (2-tailed)     | 0.437       | 0.017         | 0.022             | -                | -                 | -                 | -                   | -                     | - |

Table 7: Pearson Correlation between Ownership Structure and Total Net Asset Value

Organizational ownership structure was found to be positively and significantly associated to net asset value of the money market fund portfolio ( $r = 0.877$ ,  $p < 0.05$ ) and balanced fund portfolio ( $r = 0.940$ ,  $p < 0.05$ ). However, organizational ownership was found to be positively but not significantly associated to net asset value of the equity fund portfolio ( $r = 0.353$ ,  $p > 0.05$ ).

#### 4. Discussion

It is also evident from the results that organizational ownership structure is positively correlated to organizational performance. Similarly, Barako and Tower (2007) investigated the association between ownership structure and bank performance in Kenya. The results provided a strong support that ownership structure influence bank performance. Similarly, Kapopoulos and Lazaretou (2007) discovered that there is strong evidence that ownership structure affects firm's performance, measured by profitability. Empirical findings indicate that there is a positive relationship between profitability and ownership structure in greek firms. Hallward-Driemeier *et al.* (2006) made a research on 1,500 Chinese enterprises in five cities in order to investigate the components of the investment climate and their effects on firm performance. The survey revealed that both ownership and investment climate measures influence firm performance and more specifically productivity and growth.

#### 5. Conclusions

The study, therefore concludes that, a significant proportion of the unit trusts were non-bank owned. Further, the equity fund, money market fund, balanced fund and bond market fund were the most popular investment fund types among the unit trusts. Diversity in ownership structure of unit trusts was found to positively affect financial performance among unit trusts.

#### 6. Recommendations

The study recommends that the need to improve management style, increase investment portfolios and diversify asset investment among the unit trusts strategy to realize meaningful stability in financial performance.

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