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Corporate Governance and Performance of Companies Listed at Nairobi Securities Exchange: Does Operating Environment and Top Management Team Characteristics Influence the Relationship? Kenya

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Abstract:
The general objective of the study was to determine whether operating environment and top management characteristics influence the relationship between corporate governance and performance of companies listed at the Nairobi Securities Exchange. The study aims to add value to decision making by creating a framework that can be adopted by the Nairobi Securities Exchange and other regulatory agencies like capital market authority in designing guidelines for corporate governance practices on out how firms should be governed to counter the arising challenges that continues to hinder them from raising capital from the public to post superior performance consistent to the expectations of the shareholders. The study was guided by three theoretical foundations; Agency Theory, the Environmental Dependence Theory and the Upper Echelons Theory. This study used a positivism research philosophy. The study used a cross sectional survey. The target population for the study was drawn 66 firms listed at the Nairobi Securities Exchange. The study used both primary and secondary data which were collected using questionnaires, interviews and desk review. Data analysis took place at two levels – descriptive statistics level and inferential statistics level. The findings indicate that corporate governance, operating environment and top management team characteristics jointly and significantly influence firm performance. The implication is that firms should base on management characteristics when considering maximizing shareholders interest through corporate governance practices. This will provide an opportunity for organizations to deliver to the expectations of shareholder's interest through proper formulated strategies associated with best principles of corporate governance.

Keywords: *Corporate governance, operating environment, top management team characteristics and firm performance*

1. Introduction

Corporate governance regulations ensure transparent management of companies for efficient accountability to stakeholders. According to Gregory Zabri, Ahmadand Wah (2016), the principal characteristics of effective corporate governance include transparency which is reflected in the disclosures made by the firm. It includes the disclosure of relevant financial and operational information and internal processes of management oversight and control; protection and enforceability of the rights and prerogatives of all shareholders; and directors capable of independently approving the corporation's strategy and major business plans and decisions, and of independently hiring management, monitoring management's performance and integrity, and replacing management when necessary. The firms with weaker governance structures have to face more agency problems and managers of such firms gain more private benefits (Brunninge, Nordqvist & Wiklund, 2015). It has been noted that good corporate governance simply means good business (OEDC, 1999). Corporate governance provides a structure for directing and controlling the business with a higher level of efficiency, transparency, accountability and fairness. In addition, corporate governance practices include the decision-making and controlling processes for a business. It offers an understanding of the managerial structure of business firms, as such, top management team characteristics. The various attributes of corporate governance structure, including a board of directors, an audit committee, independent directors, various other administrative committees within a board, are factors influencing the firms' decision-making process and thus play an important role in controlling manager's discretionary power hence driving the firm to higher performance.

Empirical studies have suggested that the success of an organization seldom depends upon a single factor but rather it largely stems from the ability to reach and maintain a viable balance among a combination of different factors (Kariuki, Awino & Ogutu, 2011).Environment refers to a set of conditions defined by the surroundings that dictates how the firm adjusts to survive in relation to its competitors (Ombaka,Muindi & Machuki, 2015). Organizations in a certain operating environment work to outwit, outsmart, outmaneuver as well as outperform their rivals (Lefort, McMurray& Tesvic, 2015).Accurate information from the environment enables the firm undertake efficient governance practices to achieve their goals.Top management team characteristics refer to unique personal traits ascribed to members of top management team that are innate or learned, observable or cognitive. They are indicators of the worth that the top management team members bring to administrative situations in managing their organizations(Kinuu, 2014).Furtherwith better and sound top management, communication and reporting, inefficiencies in corporate governance practices will decrease while increasing the investor confidence in an organization and therefore enhanced overall firm performance.

The listed companies are diverse covering a range of economic activities such as agriculture commercial and services, telecommunication and technology, automobiles and accessories, banking, insurance, investment, manufacturing, construction, energy, and petroleum. They provide a suitable profile of Kenya's economy. These comparisons in the performance of the listed firms provided an opportunity for this study. In addition, these firms are required by Capital Market Authority (CMA) to keep proper records through published annual accounts. These records are available on line. The variation in performance of firms listed in Nairobi Securities Exchange can therefore be explained by their unique integration of corporate governance mechanisms, their selection of top management team and how they respond to ever changing business environment.

2. Materials

This study reviews the following theories pertinent to corporate governance, top management team characteristics, external environment and performance. These include; Agency theory (Eisenhardt, 1989; Jensen & Meckling, 1976), Environment dependency theory (Ansoff & Survillan, 1993) and the upper echelons theory (Hambrick & Mason, 1984). Agency theory which is also the overarching is based on the assumptions and philosophy that separating ownership and management leads to corporate governance issues. And it's the most discussed theory in strategic management as far as corporate governance is concerned (Shukeri, Shin & Shaari, 2012).The theory is based on the argument that board of directors as an example of corporate governance minimizes the problems that may arise due to principal who are the owners and stakeholders of the firm and the agent who are the management is because CEOs seek to increase their utility at the expense of firms by withholding effort or increasing their own compensation through self-dealing (Hendry, 2002).

The environment dependency theory presents the assumptions on the notion that organizations should continuously analyze, scan and evaluate the environmental context in which they operate with the objective of detecting any trends at early state before affecting the performance. This means that as top managers develop strategies, they will be subject to macro-environment influences and will need to continuously ensure that strategic decisions take cognizance of risks being span by the environment within which the organization operates (Ansoff & McDonnell, 1990).The theory helps the study with the argument that scanning environmental conditions and forces enhances performance of listed companies at the Nairobi Securities Exchange.

The key assumptions of the Upper Echelon theory are the argument that top management team characteristics are closely related to the cognitive and psychological elements of the executives' (Cannella, Park & Lee, 2008). This gives an organization an upper hand in developing, adapting and execution those strategies that maximize the organizational power over other competing firms. The principle of the UET recognizes that top managers' different characteristics such as age or career experiences affect their decisions on strategy and structure and it will directly affect firm's strategic choice and organizational performance (Nielsen 2010). The theory enables the study understands the role of top management team characteristics and how their potential can be harnessed to improve organizational performance.

Performance realization has become a critical function for top management and corporate governance principles as firm environments become increasingly turbulent and complex. The literature concerning how operating environment and tom management teams' characteristics plays a role in corporate governance and performance relationship have been documented with varied conclusions. For instance, Abebe (2010) empirically examine the effect of top management team (TMT) characteristics on corporate turnaround performance in declining firms under conditions of environmental stability and turbulence. Theoretical hypotheses were developed and tested using data collected from 98 US manufacturing firms that experienced performance decline and turnaround during the periods 1990-1994 and 1995-2000 respectively. Data were collected from the COMPUSTAT database and annual filings and analyzed using a moderated regression analysis. The results of moderated regression analysis indicate an adverse effect of long organizational tenure on corporate turnaround, especially in turbulent environments. Hence, if was found that the effect of top team composition on corporate turnaround varies depending on the environmental context.

Goodman, Ravlin, and Schminke (2018) indicated that the turbulence of an organization's environment moderates the association between top team size and firm performance. The more turbulent the environment, the more varied and fragmented the nature of managerial work and the greater the information-processing demands on the top team. The greater the task uncertainty, the greater the amount of information that must be processed among decision makers during task execution in order to achieve a given level of performance. Turbulent environments increase information-processing needs by creating new opportunities and crises that often necessitate strategic and structural adaptations. Hence, as an environment grows more turbulent and a firm's decision- making tasks grow more difficult, managers have greater information processing requirements.

Lester (2006) conducted an examination of top management team prestige and environmental uncertainty. Relying on one of the more notable entrepreneurial settings, an initial public offering (IPO), this article extended prior work on top management team (TMT) characteristics. The study examined whether or not prestigious TMTs at the time of an IPO enhance organizational legitimacy and thereby provide a signal to potential investors. Because an IPO represents an entrepreneurial context characterized by high levels of uncertainty, the study also considers the impact of environmental uncertainty on the TMT prestige/investor valuation relationship. The findings show that both an element of TMT prestige and environmental uncertainty influence investor valuations. However, the influence of prestige does not assuage investors when analyzing IPOs in different environmental conditions.

3. Methods

This study used a positivism research philosophy and a cross sectional survey design. The target population for the study was drawn 66 firms listed at the Nairobi Securities Exchange. The study used both primary and secondary data which were collected using questionnaires, interviews and desk review. The study used primary data collected using questionnaires. A close-ended questionnaire was used to collect primary data relating to the all variables. The questionnaire enabled the researcher to collect views of respondents on the manifestations of strategic leadership and service delivery. The questionnaire adopted a 5-likert scale. The use of 5-likert scale made it possible to quantify the qualitative data, and therefore, enable the attainment of more objective results regarding the views of respondents on the different manifestations. Before administering the data collection instrument, respondents were assured of complete confidentiality and anonymity regarding their responses. The questionnaire was administered using the 'drop and pick up later' method so as to allow the respondents ample time to respond to the questions, thereby enhancing accuracy in responses and improve response rate. For this study, both descriptive and inferential statistic (mean scores, standard deviations, percentages and frequency distribution) were used. Further the regression model was tested to depict the relationship between the dependent and independent variables. The significance of each independent variable was also tested. P-value, F-ratio and t-statistic explains the significance of the model constructs at a 95 percent confidence level.

4. Results

The study sought to establish the joint effect of corporate governance, top management team characteristics and operating environment on firm performance. Theoretical reasoning led to the belief that the joint effect of corporate governance, top management team characteristics and operating environment on firm performance is statistically significant. To assess the joint effect, the following hypothesis was tested.

- Ho_4: Corporate governance, operating environment and top management team characteristics have no any significant joint effect on the performance of companies listed at NSE.

Since the study was assessing both non-financial and financial performance, two sub hypotheses were derived from the hypothesis. The first sub hypothesis aimed at testing the joint influence of corporate governance, operating environment and top management team characteristics on the non-financial performance of companies listed at NSE. Therefore, the following sub hypothesis was tested:

- Ho_{4a}: Corporate governance, operating environment and top management team characteristics don't have any significant joint effect on the non-financial performance of companies listed at NSE. The pertinent results of hypothesis testing are displayed Table 1.

Model Summary[d]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics					Durbin-Watson
					R Square Change	F Change	df1	df2	Sig. F Change	
1	.706[a]	.498	.488	.55956	.498	47.619	1	48	.000	
2	.712[b]	.506	.485	.56069	.008	.806	1	47	.374	
3	.719[c]	.517	.486	.56061	.011	1.013	1	46	.319	1.513

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	14.910	1	14.910	47.619	.000[b]
	Residual	15.029	48	.313		
	Total	29.939	49			
2	Regression	15.163	2	7.582	24.117	.000[c]
	Residual	14.776	47	.314		
	Total	29.939	49			
3	Regression	15.482	3	5.161	16.420	.000[d]
	Residual	14.457	46	.314		
	Total	29.939	49			

Coefficients[a]						
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.934	.361		2.585	.013
	Corporate Governance	.779	.113	.706	6.901	.000
2	(Constant)	.564	.549		1.027	.310
	Corporate Governance	.747	.119	.676	6.288	.000
	Operating Environment	.132	.147	.097	.898	.074
3	(Constant)	.731	.573		1.275	.009
	Operating Environment	.162	.150	.119	1.083	.084
	Top Management Characteristics	.106	.106	.112	-1.007	.019

Table 1: Joint Effect of Corporate Governance, Top Management Team Characteristics and Operating Environment on Non-Financial Performance
a. Dependent Variable: Non-Financial Performance
b. Predictors: (Constant), Corporate Governance
c. Predictors: (Constant), Corporate Governance, Operating Environment
d. Predictors: (Constant), Corporate Governance, Operating Environment, Top Management Characteristics
Source: Research Data (2020)

The results shown in Table 1reveal that individual effect of corporate governance on non-financial performance was significant (r^2 = .498, F = 47.619, P-Value = .000<0.05). Corporate governance accounts for 49.8 percent of the variation in non-financial performance. The model was overall significant. Beta coefficient of corporate governance (β = .779, t = 6.901, p-value = 0.000<0.05) was significant. Results on joint effect indicated that 51.7 percent of the variation in non-financial performance was explained by the changes in corporate governance, top management team characteristics and operating environment. The model was overall significant (F= 16.420, P-Value = 0.000<0.05). The joint effect was greater and significant (r^2 = 0.517, F = 16.420, P-Value = 0.000<0.05) than the individual effect (r^2 = 0.498, F = 47.619, P-Value = 0.000<0.05). The hypothesis that corporate governance, operating environment and top management team characteristics don't have any significant joint effect on the non-financial performance of companies listed at NSE was rejected.

Model Summary[d]										
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics					Durbin-Watson
					R Square Change	F Change	df1	df2	Sig. F Change	
1	.652[a]	.426	.414	.55125	.426	35.574	1	48	.000	
2	.659[b]	.435	.411	.55265	.009	.756	1	47	.389	
3	.705[c]	.496	.464	.52729	.062	5.629	1	46	.022	1.097

ANOVA[a]						
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	10.810	1	10.810	35.574	.000[b]
	Residual	14.586	48	.304		
	Total	25.396	49			
2	Regression	11.041	2	5.520	18.075	.000[c]
	Residual	14.355	47	.305		
	Total	25.396	49			
3	Regression	12.606	3	4.202	15.113	.000[d]
	Residual	12.790	46	.278		
	Total	25.396	49			

Coefficients[a]						
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.983	.356		2.761	.008
	Corporate Governance	.663	.111	.652	5.964	.000
2	(Constant)	.629	.541		1.163	.251
	Corporate Governance	.632	.117	.622	5.404	.000
	Operating Environment	.126	.145	.100	.870	.389
3	(Constant)	.258	.539		.478	.635
	Corporate Governance	.558	.116	.549	4.811	.000
	Operating Environment	.058	.141	.046	.413	.682
	Top Management Characteristics	.236	.099	.269	2.373	.022

Table 2: Joint Effect of Corporate Governance, Top Management Team Characteristics and Operating Environment On Financial Performance
a. Dependent Variable: Financial Performance
b. Predictors: (Constant), Corporate Governance
c. Predictors: (Constant), Corporate Governance, Operating Environment
Predictors: (Constant), Corporate Governance, Operating Environment, Top Management Characteristics
Source: Research Data (2020)

The second sub hypothesis aimed at testing the joint effect of corporate governance, top management team characteristics and operating environment on financial performance of companies listed in NSE. Therefore, the following sub hypothesis was tested:

- H_{04b}: Corporate governance, operating environment and top management team characteristics don't have any significant joint effect on the financial performance of companies listed at NSE. The results shown in Table 4.28 reveal that individual effect of corporate governance on financial performance was significant (r^2 = .426, F = 35.574, P-Value = .000<0.05). Corporate governance accounts for 42.6 percent of the variation in financial performance. The model was overall significant. Beta coefficient of corporate governance (β = .663, t = 5.964, p-value = 0.000<0.05) was significant.

Results on joint effect indicated that 49.6 percent of the variation in financial performance was explained by the changes in corporate governance, top management team characteristics and operating environment. The model was overall significant (F= 15.113, P-Value = 0.000<0.05). The joint effect was greater and significant (r^2 = 0.496, F = 15.113, P-Value = 0.000<0.05) than the individual effect (r^2 = 0.42.6, F = 35.574, P-Value = 0.000<0.05). The hypothesis that corporate governance, operating environment and top management team characteristics don't have any significant joint effect on the financial performance of companies listed at NSE was rejected.

5. Conclusions and Implications of the Study

This study showed that the joint effect of corporate governance, top management team characteristics and operating environment on firm performance was statistically significant. This conclusion is consistent with findings from previous research and lends credence to the idea that firm performance is determined, in part, by the combination of factors both from the corporate governance, top team management and operating environment. This study has confirmed the contributions by the various theories and lends support for the hypothesized relationships. The result contributes to the strengthening of the literature by confirming the postulations of agency theory, environment dependency theory and upper echelon theory. The study therefore pointed out that for corporate governance to have meaningful relationship with performance, environment factors and top team management characteristics should be considered, controlled and streamlined with the key organizational capabilities.

Most companies listed in the NSE have previously not received best corporate governance, yet these companies are crucial to Kenya's economic development and contribution to gross domestic product. Hence this will provide a guide to policy makers to develop strategies to enhance effective corporate governance for the firms. From the findings it was evident that political environment and changes greatly affected operations in the firms. This study will hence be used by policy makers to create favourable environment for business operations as well as develop policies to govern fair competition that is corruption free.

The board, which is the management of the corporation, makes decisions about day-day operations of a firm as well as supervisory function that comprise monitoring a firm's performance and major decisions pertaining the company's objectives. Therefore, effective board size in an organization promotes innovative ideas, application of knowledge to push and integrate the corporation into the competitive global market. On management practice, effective board size should be agreed on by the directors and shareholders for effective corporate governance for better firm performance. Additionally, a good corporate governance structure should be adopted to aid companies to have access to funds and increased returns which results in an improvement in their earnings. The study should therefore form basis on how policy, managerial view and future researchers should blend the study variables applicability to recommend the best fit to different functional areas especially in listed firms for performance to be improved for economic prosperity.

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