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INFLUENCE OF CORPORATE GOVERNANCE ON FINANCIAL PERFORMANCE OF SAVINGS AND CREDIT COOPERATIVE ORGANIZATIONIN NAIROBI CITY COUNTY, KENYA

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Abstract: **The purpose of the study was to examine effect of corporate governance on financial performance of SACCOs in Nairobi city. It was guided by the following specific objective; to determine the effect directors' shareholding on financial performance. The study used agency theory, stakeholder theory and resource dependency theory. This study adopted a descriptive research design with a target population of all the senior management, middle level management and all staff of the seventeen SACCOs operating in Nairobi City County and a sample of 51 was generated by purposively sampling three employees from each SACCOs which included chief executive officer, finance manager and risk manager. This study used structured questionnaires for data collection. Collected data was cleaned and then entered into an SPSS programme for data analysis. Descriptive statistics such as percentages, mean trends and standard deviation will be computed to describe the characteristics of the variables while inferential statistics applied to establish the nature and magnitude of the relationship between the variables. Multiple regression and analysis of variance was used to test the relationship of one variable over the other. Based on the findings, the study concluded directors shareholding was found to be positively related financial performance of savings and credit cooperative organization in Nairobi City. The study will be significant to the directors of SACCOs, the government through the ministry of cooperatives and identify gaps for further research on the field.**

Keywords: **Directors Stakeholders, Financial Performance Corporate Governance.**

1. INTRODUCTION

Corporate governance in an organization is about fair, efficient and transparent administration of on organization so that in the long run it meets its set objectives thereby satisfy stakeholders and comply with legal and regulatory requirements (Linner, 2009). In matters corporate governance there is no one size that fits all (ACGN, 2016). This notion is also agreed upon by OECD (2014) who asserts that there is no single model of good corporate governance. That notwithstanding, a key underlying feature to point out is that there are some common elements that underlie good corporate governance.

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Corporate governance has implications for economic development especially in helping to increase the flow of financial capital to firms in developing countries and emerging markets. OECD (2014) opines that if countries are to reap in full the benefits of the global capital market and if they are to attract long term "patient" capital, then corporate governance arrangements must be credible, well understood across borders and adhere to internationally recognized and accepted principles. According to Okeahalam and Akinboade (2003), good corporate governance can be a valid mitigation measure for issues that would have otherwise been derived from the 'principal-agent' problem. It is of paramount importance to mention that even though corporate governance is universally practiced, there is no single model of corporate governance. The corporate governance framework depends on the legal, regulatory, and institutional environment and is affected by the relationships among participants in the governance system (OECD, 2014). Employees in a particular company or organization as well as other stakeholders play an important role in controlling shareholders and management. Okeahalam & Akinboade (2003) note that scholars from developed economies have made tremendous effort to look at the basic premise of corporate governance. In a rejoinder, ACGN (2016) reports that more literature is being generated as compared to yesteryears and that considerable research on corporate governance is now being undertaken across Africa. Nevertheless, it has to be noted that there have not been many studies on corporate governance in Africa. Better corporate governance is highly correlated with better operating performance and market valuation in Africa. A particular difficulty in Africa, in designing and implementing appropriate regulatory, enforcement and incentive regime is the lack of skills and institutional capacity to do so. There is a systemic lacuna gap lacuna from the various institutions, companies and stakeholders.

For instance, one of the earlier concerns with the upsurge in corporate governance as a key policy issue was the tendency for the researched experiences of more developed economies to inform the standards and rules that should apply universally across all economies. Egypt, one of the pioneer countries in development of corporate governance experienced support for creation of sound corporate governance frameworks came from both the private and the public sector. Corporate governance has in recent years become a topical issue both in business and academic circles. The concern in business arose out of the perceived importance that a tradition should be developed that supports moral and ethical conduct in business affairs which will create a general climate (both legal and social environment) that will promote good governance of firms. In the academic world, it is established that business decisions are not made in a vacuum. Business decision makers have objectives outside the firms' objectives, for example managers are interested in their own personal satisfaction, in their employees' welfare, as well as in the good of the community (society) at large and these objectives impact on shareholders wealth adversely (Akeem, 2014). The genesis of Corporate Governance lies in business scams and failures. The Watergate scandal, the junk bond fiasco in USA and the failure of Maxwell, BCCI and Polypeck in UK resulted into setting up of the Treadway committee in USA and the Cadbury committee in UK on corporate governance. The guiding principle of good corporate governance is "transparency and ethics" should govern corporate world. Increasing strategic importance of professional management probably constitutes the most important aspect of changing profile of corporate governance. Given the global challenges, the only choice left with business and economic enterprises is to follow the corporate governance practices – the path for living, working, surviving, successions and the excelling in the future (Bansal and Bansal, 2014).

Directors without corporate enforcement mechanism may paint misleading pictures of financial performance of their organisations to lure unsuspecting investors. However, the effect of these actions on some corporations is devastating. There is the collapse of the energy corporation Enron in 2001 in US, WorldCom, Global Crossing, and Rank Xerox, most of which filed for bankruptcy after adjusting their accounts. Between 2002 and 2005, several international corporations failed, including Mutual Risk Management Ltd, Equitable Life Assurance Society UK collapsed in year 2000 because directors of the companies unlawfully used money met for guaranteed annuity rate policies to subsidize current annuity rate policies. Lion of Africa Insurance in Nigeria also liquidated because of board crisis it liabilities outweighed the assets and could not recapitalize in 2007 (Momoh and Ukpong, 2013). The increasing incidence of corporate fraud relating to exaggerated and overstated accounts have informed renewed global emphasis on the need for good corporate governance. According to Nwachukwu (2007), there is a growing consensus that good corporate governance has a positive link to national economic growth and development. Checks and balances in an organization are strengthened through good corporate governance. By definition, corporate governance is a system or an arrangement that comprises of a wide range of practices (accounting standards, rules concerning financial disclosure, executive compensation, size and composition of corporate boards) and institutions (legal, economic and social) that protect the interest of corporation's owners.

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Furthermore, adherence to good corporate governance is inevitable especially in the Nigerian business climate considering the critical multiplier effects a failed corporate entity would cause to investment decision, unemployment rate and economic growth. Thus, the practice of a good corporate governance system helps to provide a degree of confidence that is necessary for the proper functioning of the market economy and hence organizational performance (Momoh and Ukpong, 2013). To this end, there is also a widely held view that better corporate governance is associated with better firms' performance, but the evidence is not sufficiently available in the Nigeria context. As such, providing an additional empirical evidence of the impact of good corporate governance on organizational performance is urgently needed.

When fully implemented, good corporate governance ensures that large corporations are well-run institutions that earn the confidence of investors and lenders. The corporate governance model adopted by countries such as Kenya broadly follows the market-based system evolved from the United Kingdom where the market strongly influences adherence to corporate laws and regulations however this is largely absent in Kenya (ACGN, 2016). Among the key initiatives put in place to promote development of corporate governance in Kenya include: the Constitution of Kenya, principles for corporate governance in Kenya and a sample code of best practice for corporate governance released in 2003 as well as the code of corporate governance practices for public listed companies. A Savings and Credit Co-operative (SACCO) is a democratic, unique member driven, self-help union. It is owned, governed and managed by its members who have a common bond: working for the same employer, belonging to the same church, labour union, social fraternity or living/working in the same community (KUSCO). In a cooperative society people come together voluntarily for the purpose of solving their socio-economic problems through self-help initiatives, mutual support and investment ventures aimed at equally benefiting the group and members. The most common types of co-operative societies in Kenya include but not limited to; Savings and credit co-operatives, housing co-operatives, consumer co-operatives, transport co-operatives, marketing co-operatives, horticulture co-operatives, handicraft co-operatives, industrial co-operatives, building and construction co-operatives, service co-operatives and multi-purpose co-operatives.

The SACCO industry is part of the cooperative sector in Kenya, which has impacted on lives of many disadvantaged Kenyans over the years. SACCOs in Kenya may be categorized into financial and non-financial cooperatives. Non-financial cooperatives deal with the marketing of members' produce and services such as dairy, livestock coffee, tea, handicrafts and many more similar cooperatives. On the other hand financial cooperatives comprise Saccos, housing and investment cooperatives. Despite tight regulatory framework, corporate governance continues to weaken in Kenya (Mang'unyi, 2011). According to Muriithi (2009), many companies have been characterized by scandals. The introduction of corporate governance practices in the Sacco sector in Kenya is aimed to provide a mechanism to improve investor confidence and trust in management and promote economic development of the country. However, efficiency of the corporate governance structures and practices on SACCOs operating in the highly competitive environment in Kenya has not been empirically investigated. Therefore, in order to understand the governance practices that contribute in enhancing the value of SACCOs regulated by SASRA, this study will aim at exploring the efficacy of corporate governance practices, which affect SACCOs performance resulting in accountability to shareholder and other stakeholders through appropriate corporate governance practices, which enhances the value of the SACCOs in Kenya. The SACCO sector is becoming increasingly important in Kenya. This sector is a key player in the economy, controlling about 43 per cent of Kenya's gross domestic product (GDP) and yet few researchers have researched on a direct link between corporate governance and financial performance within this sector. This therefore called for an investigation into the impact of corporate governance on the financial performance of SACCOs in Kenya. This study aims at determining the effect of directors' shareholding on financial performance of savings and credit cooperative organization in Nairobi City County.

2. EFFECT OF DIRECTORS' SHAREHOLDING ON FINANCIAL PERFORMANCE

On a broad perspective, corporate governance implies that companies not only maximize shareholder wealth, but balance these interests with those of other stakeholders which include the firm's employees, customers, suppliers as well the community within which they operate (AfDB, 2011). Good corporate governance principles offered by OECD (2014) include: protection of shareholders rights; equitable treatment of all stakeholders including effective redress; recognition of all stakeholders; timely and accurate disclosure of all matters that are regarded by a firm as being material. These may include financial, performance, ownership and governance matters. Internal factors such as concentration in shareholding play a large role in the performance of a SACCO. Large shareholders play an important role on firm performance and policies strategically influencing control of an entity(Gachunga, 2017). The shareholder control revolves around the rights of a shareholder to be able to vote and exercise control over firm assets, removal of inefficient management or effect ownership changes to increase shareholding (Gachunga, 2017).

OECD (2014) further notes that controlling shareholders, which may be individuals, family holdings, bloc alliances or corporations acting through a holding company or cross shareholdings can significantly influence corporate behavior. While individual shareholders may not seek to directly exercise governance rights, they may be particularly concerned about obtaining fair treatment from controlling shareholders and management. Shareholders should have the right to participate in and to be sufficiently informed on decisions concerning fundamental corporate changes such as amendment of statutes or articles of incorporation or similar governing documents. The essence of effective shareholder participation in key corporate governance decisions cannot be understated. For instance nomination and election of board members should be adequately facilitated so that even the individual shareholders can feel as being part and parcel of the stakeholder community. When looking at the role of shareholders and other stakeholders in holding directors and management accountable for corporate conduct, it has been largely agreed that large institutional investors wield significant influence over whether corporations are responsive to shareholder interests or not (SGFCG, 2015). An observation has been made to the effect that lately, the role of proxy advisory firms has acquired significant influence in the marketplace. Some shareholders are now going to the extent of subscribing to the advice of proxy advisors (SGFCG, 2015). Control of shareholding between the domestic and foreign owned financial institutions reveal that foreign banks have a higher loan portfolio quality and lower levels of insider lending, however also important to note is that the foreigners get more privileges in voting rights thereby increasing the risk adjustment while reducing the default risk. Research relating to block shareholding shows that as long as the major stakeholders are financial institutions and foreigners there is an improved performance (Gachunga, 2017).

Cooperatives are formed by and for members to serve their common need or goal hence the right to hold or acquire shares only arises through the individual's status as a member. There are key characteristics of cooperative share capital which include: Only SACCO members are eligible to shares. For one to qualify for shares, they need to agree to be members of the SACCO and be bound by the rules and regulations that there are in the SACCO. The SACCO rules may also include procedures to acquire more shares. For SACCOs shares do not necessarily carry a vote and in that case every member has a single vote albeit shares might vary from the different members. Another key characteristic is that shares have a fixed value which is not tradable on a stock exchange. The ability to repay capital is a feature of cooperatives that lends to issuing community shares. The dividend question is also important for cooperatives since it encourages members to leave their capital with the cooperative. Gachunga (2017) posits that a shareholder would be as much interested in wealth maximization as control of the firm. Therefore, in general, the performance of SACCOs is characterized by growth in share/deposits (Mwanja, Mwarangu, Wanjere and Thuo 2014).

3. METHOD

This study adopted a descriptive research design with a target population of all the senior management, middle level management and all staff of the seventeen SACCOs operating in Nairobi City County and a sample of 51 was generated by purposively sampling three employees from each SACCOs which included chief executive officer, finance manager and risk manager. This study used structured questionnaires for data collection. Collected data was cleaned and then entered into an SPSS programme for data analysis. Piloting was done to test the validity and reliability of the data collection instrument. Descriptive statistics such as percentages, mean trends and standard deviation was computed to describe the characteristics of the variables while inferential statistics applied to establish the nature and magnitude of the relationship between the variables. Multiple regression and analysis of variance was used to test the relationship of one variable over the other.

4. RESULTS AND DISCUSSION

4.1 Results and Discussion

The study aimed at finding out the effect of directors' shareholding on financial performance of savings and credit cooperative organization in savings and credit cooperative organization in Nairobi City. The results were then presented them in the Table 4:1.

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Table 4:1 Effect of directors' shareholding on financial performance of savings and credit cooperative organization in savings and credit cooperative organization in Nairobi City

statement	SA	A	N	D	SD	Total
Good corporate governance practices have an effect on increased shareholding on the sacco	5.0	26.0	3.0	49.0	17.0	100
Large shareholding has a direct impact on the sacco performance	48.0	33.0	5.0	12.0	2.0	100
Non violation of shareholders rights impacts on the financial performance of the sacco	10.0	49.0	3.0	34.0	4.0	100
Shareholder participation in decision making has influence on the financial performance of the sacco	48.0	43.1	1.3	6.9	0.0	100
The ability to repay capital is a feature of cooperatives that lends to issuing community shares and dividend question is also important for it encourages members to leave their capital with the cooperative	40.6	18.4	10	21	10	100

The results from table 4.1 above on whether good corporate governance practices have an effect on increased shareholding on the Sacco. 5.0 percent and 26.0 percent of the respondents strongly agreed and agreed respectively to the statement that good corporate governance practices have an effect on increased shareholding on the Sacco while 3.0 percent being neutral. 49.0 percent of the respondents disagreed and 17.0 percent strongly disagreed that good corporate governance practices have an effect on increased shareholding on the Sacco. The finding shows that majority of the respondents disagreed that good corporate governance practices have an effect on increased shareholding on the Sacco.

The results of the study sought to establish whether large shareholding has a direct impact on the Sacco performance and results were presented in Table 4:6. The results showed that majority 48.0percent agreed, 33.0 percent of the respondents agreed, 5.0 percent were neutral,12.0 percent disagreed while 2.0 percent strongly disagreed on the statement that large shareholding has a direct impact on the Sacco performance. This implied that majority 81.0percent of the respondents agreed that large shareholding has a direct impact on the Sacco performance.

The findings established whether non violation of shareholders rights impacts on the financial performance of the Sacco. Majority 10.0 percent of the respondents strongly agreed to the statement, 49.0 percent of the respondents agreed, 3.0 percent neutral while34.0 percent disagreed and 3.0 percent strongly disagreeing respectively. This results revealed clearly that majority of the respondents agreed to the statement that non violation of shareholders rights impacts on the financial performance of the Sacco.

Further, the findings established on whether shareholder participation in decision making has influence on the financial performance of the Sacco. Majority 48.6percent agreed while 6.9percent strongly disagreed, 43.1percent agreed and 1.4 percent was neutral. The results of the findings showed clearly that majority of respondents disagreed that shareholder participation in decision making has influence on the financial performance of the Sacco.

Finally, the findings established on whether the ability to repay capital is a feature of cooperatives that lends to issuing community shares and dividend question is also important for it encourages members to leave their capital with the cooperative. Majority 40.6percent agreed while 18.4 percent strongly agreed to the statement that the ability to repay capital is a feature of cooperatives that lends to issuing community shares and dividend question is also important for it encourages members to leave their capital with the cooperative, 10 percent disagreed and 21 percent of the respondents strongly disagreed to the statement that the ability to repay capital is a feature of cooperatives that lends to issuing community shares and dividend question is also important for it encourages members to leave their capital with the cooperative. Only 10 percent of the respondents were neutral. This revealed that majority of respondents agreed that the ability to repay capital is a feature of cooperatives that lends to issuing community shares and dividend question is also important for it encourages members to leave their capital with the cooperative.

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4.2 Inferential Statistics

4.2.1 Pearson Correlation

The study sought to establish the strength of the relationship between independent and dependent variables of the study. Pearson correlation coefficient was computed at 95 percent confidence interval (error margin of 0.05). Table 4.2 illustrates the findings of the study.

Table 4.2: Correlation Matrix

		Financial performance
Director's shareholding	Pearson Correlation	.711**
	Sig. (2-tailed)	.000
	N	46

As shown on Table 4.2 above, the p-value for directors shareholding was found to be 0.000 which is less than the significant level of 0.05, ($p<0.05$). The result indicated that Pearson Correlation coefficient (r-value) of 0.711, which represented a strong, positive relationship between directors' shareholding and financial performance of savings and credit cooperative organization in savings and credit cooperative organization in Nairobi City

4.2.2 Multiple Linear Regression

Multiple linear regressions were computed at 95 percent confidence interval (0.05 margin error) to show the multiple linear relationship between the independent and dependent variables of the study.

4.2.2.1 Coefficient of Determination (R^2)

Table 4.3 shows that the coefficient of correlation (R) is positive 0.634. This means that there is a positive correlation between cooperate governance and financial performance of savings and credit cooperative organization in savings and credit cooperative organization in Nairobi City. The coefficient of determination (R Square) indicates that 26.2 percent of financial performance of savings and credit cooperative organization in savings and credit cooperative organization in Nairobi City. The adjusted R^2 however, indicates that 24.1percent of financial performance of savings and credit cooperative organization in savings and credit cooperative organization in Nairobi City is influenced by cooperate governance leaving 75.9 percent to be influenced by other factors that were not captured in this study.

Table 4.3: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.634[a]	.262	.241	4.20616

A. Predictors: (Constant), Directors Shareholdings

4.2.2.2 Analysis of Variance

Table 4.4 shows the Analysis of Variance (ANOVA). The p-value is 0.000 which is < 0.05 indicates that the model is statistically significant in predicting how cooperate governance affects financial performance of savings and credit cooperative organization in savings and credit cooperative organization in Nairobi City. The results also indicate that the independent variables are predictors of the dependent variable.

Table 4.4: ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
	Regression	502.823	4	243.451	23.101	.000[b]
1	Residual	1330.110	47	13.865		
	Total	2032.933	51			

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4.2.2.3 Regression Coefficients

From the Coefficients table (Table 4.5) the regression model can be derived as follows:

$$\mathbf{Y = 35.677 + 1.441X_4}$$

The results in table 4.5 indicate that all the independent variables have a significant positive effect on financial performance of savings and credit cooperative organization in savings and credit cooperative organization in Nairobi City. The most influential variable is directors shareholdings with a regression coefficient of 1.441 (p-value = 0.000). According to this model when all the independent variables values are zero, financial performance of savings and credit cooperative organization in savings and credit cooperative organization in Nairobi City will have a score of 35.677.

Table 4.5: Regression Coefficients

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	35.677	3.634		25.243	.000
Director's shareholdings	1.441	.180	.729	5.612	.000

4.2.3 Hypothesis Testing

Ho_1: There is no significant relationship between board of directors' shareholding and savings and credit cooperative organization in Nairobi City

From Table 4.5 above, directors' shareholding (β = 1.441) was found to be positively related financial performance of savings and credit cooperative organization in Nairobi City. From t-test analysis, the t -value was found to be 5.612 and the ρ -value 0.000. Statistically, this null hypothesis was rejected because $\rho<0.05$. Thus, the study accepted the alternative hypothesis and it concluded that directors' shareholding affects financial performance of savings and credit cooperative organization in Nairobi City

5. CONCLUSIONS AND RECOMMENDATIONS

The study aimed at finding out the effect of directors' shareholding on financial performance of savings and credit cooperative organization in savings and credit cooperative organization in Nairobi City. The finding indicated that good corporate governance practices have an effect on increased shareholding on the Sacco and that large shareholding has a direct impact on the Sacco performance. The findings also established that non violation of shareholders rights impacts on the financial performance of the Sacco and that Shareholder participation in decision making has influence on the financial performance of the Sacco. It was also revealed that the ability to repay capital is a feature of cooperatives that lends to issuing community shares and dividend question is also important for it encourages members to leave their capital with the cooperative. Based on the findings, the study concluded as follows; Directors' shareholding (β = 1.441) was found to be positively related financial performance of savings and credit cooperative organization in Nairobi City. From t-test analysis, the t -value was found to be 5.612 and the ρ -value 0.000. Statistically, this null hypothesis was rejected because $\rho<0.05$. Thus, the study accepted the alternative hypothesis and it concluded that directors' shareholding affects financial performance of savings and credit cooperative organization in Nairobi City

Based on the findings, the study recommends that Sacco's should embrace the effective management of financial by ensuring enough working capital for success of their firm. They should ensure that succeeding quantitative characteristics such as understandability, significance, materiality, reliability, and substance over form, carefulness, completeness, comparability, suitability and an equilibrium between benefit and cost are met: They should practice proper planning, organizing, directing and controlling the financial actions like procurement and deployment of funds of the venture to enhance the Sacco's performance. The management of the Sacco's should also have an efficient liquidity management that requires maintaining sufficient cash reserves on hand while also investing as many funds as possible to maximize earnings . The management of the Sacco should put forth an effective dividend policy to guide the firms on deciding how much money will be paid out of members earnings to the shareholders and that investors favours stocks with stocks that

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had higher dividend pay-outs. They should not violet the organizational values of shareholders rights for the financial performance of the Sacco's for good corporate governance practices have an effect on increased shareholding on the Sacco.

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